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MUNICIPAL BONDS

MUNICIPAL BONDS

A STATEMENT OF THE PRINCIPLES OF LAW AND CUSTOM GOVERNING THE ISSUE OF AMERICAN MUNICIPAL BONDS WITH ILLUSTRATIONS FROM THE STATUTES OF VARIOUS STATES

By

FRASER BROWN

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To
FREDERICK PRIME DELAFIELD, Esq.
of the New York City Bar

FOREWORD AND ACKNOWLEDGMENT

The necessity for a book of this character became apparent during the preparation of a course of lectures on municipal bonds recently delivered at the School of Commerce, Accounts and Finance of New York University. An examination of existing literature revealed a lack of any comprehensive treatment of the subject, and suggested the present volume. The author sincerely hopes that the result of his effort will be valuable and of interest, not only to students of municipal finance, but to municipal-bond houses, public officials responsible for bond issues, and the general investor.

The literature on the subject of municipal bonds begins with the late Judge Dillon's masterly treatise on the law of municipal corporations. There is, however, an hiatus between the "Law of Municipal Corporations" and articles in various textbooks covering the general field of investments, and casual articles by investment bankers.

The general principles of municipal-bond law can be stated for the student and the "bond man." The adoption of the Uniform Negotiable Instruments Law by all the States (except one) has inevitably tended to produce more or less uniform decisions on mooted points. While there are curious decisions in many jurisdictions, it is probably true that these decisions are the result of hard facts, which are said to make bad law. Generally speaking, fundamental canons have been worked out and further judicial decisions must tend more and more toward recognition of established rules. The work of the legal specialist is statutory construction.

An attempt is made in the following pages to treat the fundamental principles of the subject clearly and concisely, leaving to the specialist the application of such principles and the consideration of the law of the jurisdiction applying to particular issues of securities.

If much of the material is quoted or taken from the "Law of Municipal Corporations," it is because that treatise has done

for the law of municipal corporations what Bishop did for the law of domestic relations, and what Whigmore has done for the law of evidence. Numerous citations and direct and indirect quotations from "Ruling Case Law" seem justified because it is unnecessary to re-state principles of law which have been adequately stated in that digest.

Acknowledgment is due to my associate, Lewis L. Delafield, Jr., Esq., for kindly criticism and advice, and to other associates, who have verified citations and read the proofs of this book. Acknowledgment is not complete without an expression of great appreciation of the counsel, encouragement and example of the associate to whom this book is dedicated.

FRASER BROWN.

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County, kept in the office of the County Collector, and such registration shall be noted on the back of this bond, after which no valid transfer of this bond shall be made except on said books.

THE ORIGINAL OPINION OF MESSRS. HAWKINS, DELAFIELD & LONGFELLOW RELATIVE TO THE LEGALITY OF THE WITHIN ISSUE AND LEGAL PAPERS ARE FILED FOR THE INSPECTION OF THE HOLDER HEREOF, WITH THE UNITED STATES MORTGAGE AND TRUST COMPANY, 55 CEDAR STREET, NEW YORK.

I HEREBY CERTIFY THAT AT THE REQUEST OF THE HOLDER OF THE WITHIN BOND, FOR ITS CONVERSION INTO A BOND REGISTERED AS TO BOTH PRINCIPAL AND INTEREST, I HAVE THIS DAY CUT OFF AND DESTROYED ..... COUPONS ATTACHED THERETO, NUMBERED FROM ..... TO ..... INCLUSIVE, OF THE AMOUNT AND VALUE OF TWENTY-FIVE DOLLARS ($25.00) EACH, AMOUNTING IN THE AGGREGATE TO ..... DOLLARS $ ..... AND THAT THE WITHIN BOND IS HEREBY CONVERTED INTO A REGISTERED BOND, WITH THE PRINCIPAL THEREOF AND SEMI-ANNUAL INTEREST THEREON PAYABLE TO ..... ASSIGNEE OR LEGAL REPRESENTATIVE.

DATED, ... 19 .....

COUNTY COLLECTOR.

DATE OF REGISTRY.	NAME OF REGISTERED HOLDER	REGISTERED BY

UNITED STATES OF AMERICA

NUMBER 0000

STATE OF NEW JERSEY

NUMBER 0000

$1000

$1000

County of Hudson

TEMPORARY NEWARK TURNPIKE IMPROVEMENT BOND

County of Hudson, *a body politic and corporate of the State of New Jersey, hereby acknowledges itself indebted for value received and promises to pay to the bearer, or, if this bond be registered, to the registered holder hereof, on the first day of May, 1924, the sum of*

ONE THOUSAND DOLLARS

and to pay interest thereon at the rate of five per centum (5%) per annum, payable on the first days of May and November in each year until maturity, upon surrender of the annexed coupons as they severally become due, or, if this bond be registered as to both principal and interest, to the registered holder hereof. Both principal and interest of this bond are payable in gold coin of the United States of America of or equal to the present standard of weight and fineness, at the office of the County Collector of Hudson County, Jersey City, New Jersey.

This bond may be registered as to principal by the holder in his name on the books of the County, kept in the office of the County Collector, and such registration shall be noted on the back of this bond, after which no valid transfer of this bond shall be made except on said books until after registered transfer to bearer. Such registration shall not affect the negotiability of the coupons which shall continue to pass by delivery. At the request of the holder, this bond will be converted into a bond registered as to both principal and interest and the coupons annexed hereto detached and canceled and thereafter both principal and interest shall be payable to the registered holder.

This bond is issued for the purpose of temporarily financing Three hundred and fifty thousand dollars ($350,000.) of the cost of the Newark Turnpike Improvement, which purpose has not yet been carried out, by virtue of a resolution of the Board of Chosen Freeholders of the County of Hudson, adopted on the eighth day of May, 1919, and in pursuance of an Act of the Legislature of the State of New Jersey, entitled: "An Act to authorize and regulate the issuance of bonds and other obligations, and the incurring of indebtedness, by county, city, borough, village, town, township, or any municipality governed by an improvement commission," approved March 22, 1916, constituting Chapter 252 of the Laws of 1916, as amended.

It is hereby certified and recited that all the conditions, acts and things required by the Constitution and Statutes of the State of New Jersey to exist, to have happened and to have been performed, precedent to and in the issuance of this bond exist, have happened, and have been performed, and that the issue of bonds of which this is one, together with all other indebtedness of said County, is within every debt and other limit prescribed by the Constitution and Laws of said State.

IN WITNESS WHEREOF, County of Hudson has caused this bond to be signed by the Director of the Board of Chosen Freeholders of said County and by the County Collector under the seal of the Board, attested by the Clerk of said Board, and the coupons attached hereto to be authenticated by the facsimile signature of said County Collector and this bond to be dated the first day of May, 1919.

ATTEST

SPECIMEN

Clerk of the Board of Chosen Freeholders

Director of the Board of Chosen Freeholders

SPECIMEN

County Collector

to be authenticated by the facsimile signature of said County Collector and this bond to be dated the first day of May, 1919.

ATTEST:

SPECIMEN

Clerk of the Board of Chosen Freeholders.

Director of the Board of Chosen Freeholders.

SPECIMEN

County Collector.

HAMILTON BANK NOTE CO., N.Y.

MUNICIPAL BONDS

Chapter I

THE PROBLEM STATED

Origin of municipal bond.—The municipal bond is a creature of law. There is no other security which to the same extent as the municipal bond owes its incidents to law and not only to law but to statutory law. The origin of a municipal bond is a statute, or more than one statute. Its terms, its effect, its means of payment, are all statutory. There is no other written instrument, except the promissory note and the last will and testament, which depends so much for its vitality upon statute law.

While statutes governing the issue of bonds differ greatly among themselves, there is, and always must be, a certain similarity and agreement in principles, because such statutes aim to produce substantially the same result. General principles can be deduced from a study of statutes and decisions of the courts, construing fiscal legislation.

To form any right judgment on a municipal bond, a knowledge or at least an understanding of principles is necessary. Unless we clearly understand what a municipal corporation is, what its financial powers are, how it raises its money, and how it pays its debts, we can have no intelligent appreciation of the circumstances which make its bonds worth much or little.

Early importance of municipality.—With the political history, even with the history of the growth and development of municipalities, we are not particularly concerned. Our interest is with the present and immediate future. We may, however, note in passing that the city (the municipality) is older than the state or the nation. The glory that was Greece and the grandeur that was Rome, was the glory of

Athens and the grandeur of the Eternal City, not of well-defined nations with clearly limited frontiers. Paris was a great lady before modern or even medieval France arose to do her homage. London lay before the spires of Westminster before the Welsh marches or the Scottish border knew the King's peace. New York, Boston and Philadelphia were relatively metropolitan before thirteen sovereign and independent commonwealths gathered to form the United States.

As man emerged from the savage state, his relative weakness and lack of natural offensive members developed the need of mutual aid and protection. Groups of families formed villages in the remote past as today. The close association of human beings with fixed habitations and common necessities developed needs which could and can be met only by co-operation. A large and dense collection of human beings occupying a limited area have needs peculiar to themselves, which create the necessity for municipal or local government and regulation, and thus in its turn the necessity for corporate organization.

What those needs are we know in a general way, but we must give them passing consideration. How those needs are met it will be our secondary purpose to ascertain. The result of such needs expressed in terms of today is municipal debt. The evidences of such debt are the subject of our inquiry.

Origin of bond issue.—A bond issue has its origin in the necessity for borrowing money. When a municipal corporation decides to undertake a public improvement such as the construction of a water supply system, it borrows the money to pay the cost. It borrows because the cost is usually too great to be raised in one year from current taxes.

Suppose that a small city raises by tax each year five hundred thousand dollars to pay its expenses. Its tax rate may be two dollars and fifty cents for each hundred, or twenty-five dollars for each thousand dollars of taxable property. The assessed valuation of taxable property in such a city, having the assumed tax rate and budget, is twenty million dollars. If it becomes necessary or desirable to expend two hundred and fifty thousand dollars on its water supply system, the effect on the tax rate of raising all the money in one year would be to increase it to three dollars and seventy-five cents a hundred or thirty-seven dollars a thousand. This exceeds the rate of tax which can be endured by property assessed at

its full cash value. Hence the money for the water supply system must be borrowed and repaid in installments.

As evidence of the borrowing, the city authorizes its proper officers to execute and deliver promises to repay the borrowed money at a definite time. Such instruments are called bonds and are negotiable instruments, on which interest is payable at an agreed rate per annum.

It not infrequently happens that the necessity for a bond issue arises from pressure exerted by local banks. The annual municipal revenues may have fallen short and the deficiency of taxes may have forced the municipality to borrow to meet its running expenses. Obligations issued in anticipation of current revenues ought not to be funded and may not be, in States having proper fiscal statutes. But appropriations may have been made for capital expenditures, and local banks may have loaned the city money for a short period until taxes are collected, or bonds can be issued.

The impulse to issue bonds may come when a bank examiner calls the attention of the bank to the fact that it holds too much city paper—an amount beyond the limit which it is legally authorized to lend or an amount too great in relation to its assets.

Preliminary steps.—The necessity having arisen and the initiative having been taken by the executive, the financial officer or officers consult the law-making body, such as the city council in second class cities in New York State. Ordinarily the city council has a committee on finance, the members of which have had little or no experience with, or understanding of, financial problems. Nevertheless, the finance committee meets and confers with the financial officials and it is agreed that bonds must be issued. In short, the finance committee agrees to recommend the passage of appropriate local legislation, that is, the ordinance or resolution authorizing the bonds.

Then the delegated officials confer with the corporation counsel and the latter consults with counsel who makes a specialty of municipal business. At this conference the facts are laid before counsel. The interest rate which the proposed bonds are to bear is frequently determined after consultation with the representatives of the better class of investment banking houses, the term or length of time the bonds are to run is computed, and other details are arranged.

Ordinance authorizing bond issue.—An ordinance authorizing the bonds is next prepared and a draft submitted to the local authorities for consideration. If satisfactory in form, it is introduced in the local legislative body. If the majority of the council be of the same political faith as the officials in charge of the matter, the ordinance is made an administration measure and all the members of the council of that particular political party retire around a corner and "caucus." The minority members retire around another corner and likewise "caucus." Then it shortly appears in the newspapers that the majority party, being possessed of all the wisdom, all the intelligence and all the administrative ability of the nation, as locally represented, is about to introduce an ordinance for the issue of bonds.

We will assume that the ordinance is introduced, properly approved in caucus and adopted by the necessary vote. A two-thirds or larger vote is frequently required. Counsel then prepares the necessary resolution prescribing the form and contents of the bond and setting forth the notice of sale which must be published.

Printing.—If the market is fairly stable and the interest rate can be regarded as settled, it is usually advisable at this point actually to prepare—that is, engrave or print—the bonds themselves. The practice of engraving municipal bonds has practically disappeared. They are printed on tinted sheets with steel-engraved borders and the perfection of printing is such that, everything considered, a type-printed bond makes a better looking instrument. Regarding coupons, experience shows that they should be reproduced by photolithography to obtain the best results.

Publication of notice.—Public sale of the bonds is usually required. This means that a notice must be published describing the proposed issue by its amount, interest rate, maturity, and the like, and stating that the bonds of the issue will be offered for sale at a specified time and place. During periods of daylight-saving time it has been found helpful to specify which variety of time is meant. The notice of sale contains all the provisions which an intending bidder needs to know and usually calls for sealed offers or proposals for the purchase of the bonds which must be accompanied by a certified good-faith check for a stated percentage, usually two per cent of the amount of the issue. The notice should be,

and is sometimes required to be, published in a metropolitan financial paper.

Sale.—The zero hour having arrived, representatives of interested bond houses meet the municipal officials in charge of the matter at the place of sale. After the bids have been received and opened for consideration, a list is prepared and the highest bidder determined. A resolution awarding the bonds to the successful bidder is then adopted.

When the bonds are prepared and ready for delivery, the purchasing bond house is notified. Counsel is requested to say whether or not the bonds can be taken up. When all is ready, a representative of the purchaser meets with the financial officer in charge of the delivery and brings with him a certified check to pay for the bonds—the amount of which check has previously been determined—and the bonds are counted, examined as to signatures, delivered, and paid for.

With the merchandising of the bonds—the sale by the dealer to the ultimate holder or investor—this book has no concern. The various kinds of municipal bonds which find a place in the market and the numerous elements which determine the price at which such bonds can be sold under ordinary conditions are, however, discussed.

Municipal ordinances and budgets.—Reference has been made to the budget and to the bond ordinance or resolution. A preliminary reading of a municipal tax ordinance, budget, and bond ordinance, and consideration of the form of each, will be helpful to an understanding of the discussions of principles. The tax ordinance is the written legislative act of the local board or body having the power to levy taxes, which provides for the levying of a tax for municipal purposes and specifies in general terms the objects for which the tax is levied. The budget specifies in detail how the amount of tax is to be expended. The bond ordinance is the legislative act of the municipality, authorizing the issue of bonds. Forms of each of these documents follow this chapter.

Tax Ordinance of the City of Clifton, New Jersey, for the Year 1922

AN ORDINANCE RELATING TO TAXES FOR THE YEAR NINETEEN HUNDRED AND TWENTY-TWO

BE IT ORDAINED, by the City Council of the City of Clifton that there shall be assessed, raised by taxation and collected for the fiscal year 1922 the

sum of Six Hundred Twenty-Six Thousand, Four Hundred Twenty-Three Dollars and Ninety Cents ($626,423.90), for the purpose of meeting the appropriations set forth in the following statement of resources and appropriations for the fiscal year 1922.

RESOURCES

Surplus Revenue Appropriated	None
Miscellaneous Revenues	$ 76,900.00
School Monies from State, School Balances, etc.	102,000.00
Revenue from other sources than Taxes	$178,900.00

APPROPRIATIONS

Appropriations in City Budget	$397,702.76
Appropriations for School Purposes	387,150.00
Overexpenditure of Appropriations, 1921	18,053.65
Deficit Surplus Revenue, 1921	2,417,49
	$805,323.90
Revenue from other sources than Taxes	178,900.00
Net amount to be raised by Taxation	$626,423.90

Budget of the City of Clifton, N. J.

For the Fiscal Year Beginning January 1, 1922, and Ending December 31, 1922

ANTICIPATIONS

	1922
Surplus Revenue	None
Surplus Revenue Appropriated	None

MISCELLANEOUS ANTICIPATED:

Fees and Permits	$ 4,000.00
Fines and Penalties	4,000.00
Health Permits	3,000.00
Franchise Tax	40,000.00
Gross Receipts Tax	6,500.00
Interests and Costs	7,100.00
Licenses	4,300.00
Poll Tax	2,000.00
Auto Bus Receipts	6,000.00
	$ 76,900.00
Amount to be raised by Taxation	320,802.76
	$397,702.76

APPROPRIATIONS

	1922
GENERAL GOVERNMENT:	
Administrative and Executive	$ 16,000.00
Assessment and Collection of Taxes	9,200.00
Department of Finance	1,200.00
Interest on Current Loans	7,000.00
Grounds and Buildings	4,500.00
Advertising, Printing and Office Supplies	5,500.00
PRESERVATION OF LIFE AND PROPERTY:	
Police	65,000.00
Police Pension Fund	2,600.00
Fire	28,500.00
Rental of Hydrants	5,000.00
HEALTH AND CHARITIES:	
Health	7,000.00
Charities	500.00
Poor	5,000.00
STREETS, HIGHWAYS AND SEWERS:	
Cleaning and Maintenance of Streets	20,000.00
Street Improvement Liabilities 1921, 1920, 1919	25,302.80
Garbage and Ashes	12,500.00
Lighting of Streets	17,500.00
Trees	1,000.00
Engineering Department	14,000.00
County Bills unpaid 1920-1921	32,298.15
EDUCATION:	
Library	4,000.00
DEBT SERVICE:	
Payment of Bonds	30,000.00
Payment of Sinking Fund	13,936.26
Interest on Bonds	59,700.00
School Construction in excess of bond issue	465.55
CONTINGENCIES	10,000.00
	$397,702.76

School Bond Ordinance for the City of Camden, N. J.

AN ORDINANCE AUTHORIZING THE ISSUE OF $1,000,000 SCHOOL BONDS OF THE CITY OF CAMDEN AND PROVIDING FOR THEIR PAYMENT

RECITALS:

Pursuant to due action by the Board of Education and the Board of School Estimate an appropriation has been requested for certain school purposes as follows:

Purpose	*Cost*
Building and furnishing two new fireproof school houses	$ 385,000
Building and furnishing additions to three non-fireproof school houses	425,000
Building fireproof administration building and stockroom	50,000

Purpose	*Cost*
Furnishing machine shop in new high school.....	65,000
Constructing cement sidewalks and fences for all schools....	75,000
	$1,000,000

It is advisable to issue bonds to provide funds for said purposes in pursuance of an Act of the Legislature of the State of New Jersey entitled: "An Act to establish a thorough and efficient system of free public schools, and to provide for the maintenance, support and management thereof," approved October 19, 1903, as amended.

The average of the different periods assigned by said statute for the maturity of bonds issued for said purposes, taking into consideration the amount of bonds to be issued as herein provided for said several purposes, is thirty-three (33) years.

BE IT ORDAINED BY THE CITY COUNCIL OF THE CITY OF CAMDEN:

SECTION 1. School bonds of the City shall be issued in the aggregate principal amount of $1,000,000, shall be dated May 1, 1922, and $30,000 thereof shall mature on May 1 in each of the years 1923 to 1945 inclusive and $31,000 thereof shall mature on May 1 in each of the years 1946 to 1955 inclusive. Said bonds shall bear interest at the rate of five per centum (5%) per annum, payable semi-annually on May 1 and November 1 in each year, shall be of the denomination of $1,000 each, and shall be in such form as may be provided by resolution.

SECTION 2. Said bonds shall be sold at public sale as provided by law, or if no bids are received at public sale, then at private sale.

SECTION 3. In each year after the issuance of said bonds, the City shall in its annual tax levy raise money sufficient to pay the interest and principal of such bonds as may mature during such year.

SECTION 4. This Council does hereby concur in and consent to the appropriation referred to in the preambles hereof, and to the issuance of the bonds herein authorized.

SECTION 5. All ordinances and parts of ordinances in conflict herewith are hereby repealed. This ordinance shall take effect immediately.

Chapter II

THE MUNICIPAL BOND

Conditions of negotiability.—Generally speaking, bonds are not negotiable instruments. This is probably true without qualification as to the bonds of individuals, and the exception is in the case of bonds issued by various bodies corporate and politic. The development of modern business has made it necessary that these obligations should be easily and readily transferable, and that purchasers should take them free of all latent equities.

The municipal coupon bond payable to bearer or order is a negotiable instrument, having all the attributes of negotiable paper under the law merchant and the uniform negotiable instruments laws of the various States. The United States Supreme Court has said: "Obligations of municipalities in the form of these in suit here are placed, by numerous decisions of this Court, on the footing of negotiable paper. They are transferable by delivery and, when issued by competent authority, pass into the hands of a bona fide purchaser for value before maturity, freed from any infirmity in their origin";[1] and whenever the question has arisen, it has been so decided where the bond has been properly drawn.

The conditions of negotiability, so far as applicable to municipal bonds, are:

A. The instrument must be in writing and signed by the maker or drawer,
B. It must contain an unconditional promise or order to pay a certain sum of money,
C. On demand, or at a fixed or determinable future time,
D. To order or bearer.

Brief consideration will show that a municipal bond, payable to bearer or order, has all the elements of negotiable paper. It remains a "negotiable instrument" if registered,[2]

[1] *Cromwell v. Sac* (1877), 96 U. S. 51.
[2] Daniels, p. 1683; *D'Esterre v. New York* (1900), 104 Fed. 605.

but if properly registered, its negotiable character may be said temporarily to be suspended.[3]

Bona fide purchaser has good title.—The incidents and consequences of such negotiability need not be fully considered here, and belong indeed to the study of negotiable instruments, as such. For our particular purposes, it is important only to note that there is no defense to a suit for payment of a negotiable instrument (valid in its inception) in the hands of one who has acquired it before maturity, for value and without notice of any defenses. The settled rule of commercial law is that one is a bona fide purchaser of negotiable paper (such as is a properly drawn and issued municipal bond) who takes it before maturity and without notice of equities, and such purchaser is said to obtain a perfect title. One who purchases from a bona fide holder gets as good a title as the seller had.

Instrument void in inception never valid.—It must be kept in mind, however, that the protection afforded a bona fide holder of a negotiable municipal bond does not validate an instrument which is void in its inception; that is, a bond which the municipality has no power to issue. The analogy between such a bond and the promissory note of a lunatic is perfect. A lunatic after "office found," that is, after a sheriff's jury has declared the individual to be "non compos mentis," has no power whatsoever to make a contract. Hence a lunatic (after "office found") cannot make a valid promissory note. Whatever the instrument is, it is not a negotiable instrument with the attributes of negotiability.

Different forms of bonds.—The form of a municipal coupon bond, registerable at the option of the holder as to principal only or as to both principal and interest, with its coupons, conversion certificate and registration gridiron, follows this chapter. Such bond is payable to bearer and hence is transferable by delivery. If the owner so desires, it may be registered as to principal in his name, after which registration it is payable only to the person in whose name it is registered, until such registration is changed. The owner may also cause it to be fully registered, that is, as to interest as well as to principal. If this is to be done, the coupons are detached and cancelled and the fact noted on the conversion certificate.

[3] *Switzerland v. R. R.* (N. Y., 1912), 152 App. Div. at 75.

Forms of coupon and registered bonds used in New York follow the New Jersey form first referred to. The peculiarity of a New York coupon bond is that while it may be fully registered—that is, as to both principal and interest—it may not be registered as to principal only. A bond in the form first given may be registered as to principal only and the coupons may continue to pass by delivery as they are not affected by such registration.

The narrative of a bond.—The narrative of a bond begins with the name of the promising corporation which should always be its correct legal corporate title. A mere misnomer does not in most, if not all, jurisdictions affect the validity of the instrument but it is apt to make the draftsman feel foolish. Some cities have curious names. Trenton, New Jersey, for instance, is "The Inhabitants of the City of Trenton." Hoboken, no longer having a council, and whose mayor is only such for ceremonial purposes, is legally known as "The Mayor and Council of the City of Hoboken." New York City was until recently "The Mayor, Aldermen and Commonalty of the City of New York." Apparently everybody but the mayor and aldermen constituted the common herd.

The present tendency is toward short names, and many municipalities, particularly in New Jersey, have taken advantage of the permission contained in general statutes to shorten their long and unwieldy titles.

The clause "for value received" deserves consideration. No contract is valid without a consideration—something paid or done to induce the promise to be made. If the maker of the promise—that is, the bond—says it has "received value," it will not be heard to deny the truth of the statement.

Next comes the promise to pay to the bearer of the bond a designated sum of money, usually one thousand dollars, on a definite date and to pay interest at a specified rate per cent at certain times. The medium of payment, that is whether gold coin, lawful money, or whether payable in New York exchange, is stated, as is also the place of payment.

Parenthetically we may note that the bond differs from most other bonds in that it does not begin with "Know all men by these presents." This expression went out of fashion some years ago, and now obtains only in localities where legal verbiage is more important than legal effect.

Registered versus coupon bonds.—The covenant as to

registration follows. Until recently (although of late years the individual investor has acquired prominence as a purchaser of municipals) savings banks, insurance companies and trustees were the purchasers of most municipals, and preferred to have their bonds registered, thus making it unnecessary for their officers and agents to cut coupons and acquire the coupon thumb. The real purpose was to suspend negotiability, in order to protect their securities from theft. The individual investor wants coupon bonds, which are transferable by delivery, and the ownership of which is not evidenced by registration.

The description of the issue ordinarily sets out its principal amount and maturities. This is followed by a reference to the statute which authorizes the issue of the bond and ordinarily a reference to local legislation.

Dillon's estoppel clause.—The value of such a clause is great, for it means that all acts and things necessary to be done have been done in a legal manner. An estoppel is not, however, complete protection, for the officer signing the bond must have authority to make it and no recital can make up for an entire lack of authority. This should always be kept in mind by the prospective bond purchaser.

"If a municipal corporation, having general authority to issue bonds for specified purposes, puts forth a negotiable municipal bond issued for a lawful purpose, and therein recites, through its duly authorized officials, whose province and duty it is to ascertain and peculiarly to know the facts, compliance with the specific provisions of the law essential to the issuance of the bond, the municipality is, as against a bona fide holder of the bond, purchasing for value, and on faith of the recitals, estopped to deny the truthfulness of the recitals." [4]

"Nothing is better settled than this rule—that the purchaser of bonds, such as these, is held to know the constitutional provisions and the statutory restrictions bearing on the question of the authority to issue them; also the recitals of the bonds he buys; while, on the other hand, if he act in good faith and pay value, he is entitled to the protection of such recitals of facts as the bonds may contain." [5]

The face of the bond ends with the testimonium, or name

[4] *Town of Climax v. Burnside* (Ga. 1920), 150 Ga. 556; 104 S. E. 435.
[5] *Lake Co. v. Graham* (1888), 130 U. S. 674 at 680.

of the promissor, and statement of the official character of the officers signing the instrument, the date of the instrument, the signatures of the officers and the corporate seal.

The coupons attached call for the payment of a definite sum, usually a half year's interest, on a definite date and they are separate and independent promises to pay and in themselves constitute negotiable instruments.

On the back of the bond, ordinarily called the panels, the conversion certificate usually appears, and the registration gridiron, the purposes of which are obvious.

Municipal bond rarely secured by lien on specific property.—In conclusion, it should be noted that the municipal bond is rarely secured by a lien on specific property. A lien in the strict legal sense is the right of a creditor to sell property belonging to the debtor to satisfy the debt. Many bonds of private corporations are liens on real estate but a municipal bond, payable as we shall see from moneys raised by taxation, is a lien upon nothing, not even on the general revenues of the municipality issuing it. The means of obtaining funds to pay the bond and the remedy of the bondholder in case of default are discussed in subsequent chapters.

Form of New Jersey Coupon Bond, Registerable as to Principal Only or as to Both Principal and Interest

No. $1,000.

STATE OF NEW JERSEY, THE CITY OF CAMDEN
SCHOOL BOND

The City of Camden, a municipal corporation of the State of New Jersey, for value received, promises to pay to the bearer of this bond, or if it be registered, to the registered holder on the first day of May, 19 , the sum of one thousand dollars ($1,000.) and to pay interest thereon at the rate of four and one-half per centum (4½%) per annum, semi-annually on the first days of May and November in each year from the date of this bond until it matures, upon presentation and surrender as they severally mature of the coupons therefor annexed hereto, or if this bond be registered as to both principal and interest, then to the registered holder. Both principal and interest of this bond will be paid in lawful money of the United States of America, at the office of the City Treasurer of said City.

This bond may be registered as to principal by the holder in his name on the books of the City, kept in the office of the City Treasurer, and such registration shall be noted on the back of this bond, after which no valid transfer of this bond shall be made except on said books until after registered transfer to bearer. Such registration shall not affect the negotiability of the coupons

which shall continue to pass by delivery. At the request of the holder, this bond will be converted into a bond registered as to both principal and interest and the coupons annexed hereto detached and cancelled and thereafter both principal and interest shall be payable only to the registered holder.

This bond is one of an issue, the authorized principal amount of which is $1,000,000, the bonds of which are of like tenor, except as to maturity, and is issued pursuant to an Act of the Legislature of the State of New Jersey, entitled: "An Act to establish a thorough and efficient system of free public schools and to provide for the maintenance, support and management thereof," approved October 19, 1903, and the acts amendatory thereof and supplemental thereto, and an ordinance of said City entitled: "An Ordinance authorizing the issue of $1,000,000 School Bonds of the City of Camden and providing for their payment" duly adopted April 13, 1922, and published as required by law.

It is hereby certified and recited that all conditions, acts and things required by the Constitution and Statutes of the State of New Jersey to exist, to have happened and to have been performed, precedent to and in the issuance of this bond exist, have happened, and have been performed, and that the issue of bonds of which this is one, together with all other indebtedness of said City, is within every debt and other limit prescribed by the Constitution and Statutes of said State.

IN WITNESS WHEREOF, the City of Camden has caused this bond to be signed by its Mayor and City Comptroller under the seal of the City and attested by the City Clerk and the coupons hereto annexed to be authenticated by the facsimile signature of the City Treasurer and this bond to be dated the first day of May, 1922.

.....
Mayor

.....
City Comptroller

Attest:

.....
City Clerk

Form of Coupon

No. $22.50

The City of Camden, a municipal corporation of the State of New Jersey, will pay to the bearer on the 1st day of....., 19...., the sum of Twenty-two and 50/100 Dollars ($22.50) in lawful money of the United States of America, at the office of the City Treasurer of said City, being six months interest then due on its School Bond dated May 1, 1922, and bearing No.....

.....
City Treasurer

Certificate of Registration

I hereby certify that at the request of the holder of the within bond, for its conversion into a bond registered as to both principal and interest, I have this day cut off and destroyed.....coupons attached thereto, numbered from.....to....., inclusive, of the amount and value of Twenty-two and 50/100 Dollars ($22.50) each, amounting in the aggregate to .....Dollars ($.....), and that the within bond is hereby converted into a registered bond, with the principal thereof and semi-

annual interest thereon payable to....., assignee or legal representative.

Dated....., 19.....

.....
City Treasurer

The within bond has been registered as follows:

Date of Registry	Name of Registered Holder	Registered by

Form of New York Coupon Bond, Registerable Only as to Both Principal and Interest

No. 1 $1000.

UNITED STATES OF AMERICA, STATE OF NEW YORK,
COUNTY OF WESTCHESTER, VILLAGE OF RYE
WATER BOND

The Village of Rye, a municipal corporation of the State of New York, for value received promises to pay to bearer, or if this bond be registered, to the registered holder hereof, on the first day of December, 1922, the sum of One Thousand Dollars ($1000), and to pay interest thereon at the rate of five per centum (5%) per annum, payable semi-annually on June 1 and December 1 in each year, upon presentation and surrender as they severally mature, of the coupons therefor annexed hereto, or if this bond be registered, then to the person in whose name it is registered. Both principal and interest of this bond are payable in lawful money of the United States of America at the office of the Village Treasurer.

This bond may be converted into a registered bond, as provided by the General Municipal Law, and be registered on the books of the Village, and thereafter is transferable only upon presentation to the Clerk thereof with a written assignment duly acknowledged or proved. Upon presentation thereof, with such assignment, the Clerk will note such transfer on this bond and on said books.

This bond is one of an issue of $10,000 bonds of like date and tenor, except as to denomination and maturity, numbered from 1 to 100 inclusive, issued pursuant to the provisions of the Village Law, constituting Chapter 64 of the Consolidated Laws of the State of New York, and a proposition adopted at an election held in said Village on November 8, 1921, and a resolution of the Board of Trustees of said Village adopted November 10, 1921.

It is hereby certified and recited that all conditions, acts and things required by the Constitution and Statutes of the State of New York to exist, to have happened and to be performed precedent to and in the issuance of this bond exist, have happened and have been performed, and that the issue of bonds of which this is one, together with all other indebtedness of said Village, is within every debt and other limit prescribed by the Constitution and Laws of said State.

IN WITNESS WHEREOF, the Village of Rye has caused this bond to be signed by its President and its Village Treasurer and the corporate seal of

said Village to be hereunto affixed and attested by its Village Clerk and the coupons hereto attached to be authenticated with the facsimile signature of its Village Treasurer, and this bond to be dated December 1, 1921.

President
Village Treasurer

ATTEST:
Village Clerk

(Corporate Seal)

Form of Coupon

No. $

The Village of Rye, a municipal corporation of the State of New York, will pay to the bearer on the first day of June, 1922, the sum of Twenty-five ($25.) Dollars, in lawful money of the United States of America at the office of the Village Treasurer, being six months' interest then due on its Water Bond, dated December 1, 1921, bearing Number 1.

Village Treasurer

Conversion Certificate

WE HEREBY CERTIFY that upon the presentation of the within bond with a written request by the owner thereof for its conversion into a registered bond, we have this day cut off and destroyed coupons attached thereto, numbered from.....to.....inclusive, of the amount and value of Twenty-five ($25.) Dollars each, amounting in the aggregate to .....Dollars, and that the interest at the rate of five per centum (5%) per annum, payable semi-annually on June 1 and December 1 in each year, as was provided by the coupons, as well as the principal, is to be paid to..... .....legal representatives, successors or assigns, at .....the place stated in the coupons.

Dated,....., 19....

President
Village Treasurer
Village Clerk

Registration Certificate

IT IS HEREBY CERTIFIED that the within bond was this day registered in the name of the payee above named in the books kept in the office of the Village Clerk of the Village of Rye, and is transferable only upon presentation to said Clerk with a written assignment duly acknowledged or proved, at which time the name of the assignee shall be entered hereon and in said books by said Clerk.

IN WITNESS WHEREOF, I have hereunto set my hand and official seal this.....day of....., 19....

Village Clerk

This Bond is Registered as Follows:

Date of Registration	Name of Registered Holder	Village Clerk

Form of New York Registered Bond

No. 1 $1000

UNITED STATES OF AMERICA, STATE OF NEW YORK,
COUNTY OF ROCKLAND, VILLAGE OF SUFFERN
PAVING BOND

The Village of Suffern, a municipal corporation of the State of New York, hereby acknowledges itself indebted and for value received promises to pay to John Doe, legal representatives, successors or assigns, the sum of One Thousand Dollars ($1000) on the first day of December, 1922, with interest thereon from the date hereof at the rate of five per centum (5%) per annum, payable semi-annually on June 1 and December 1 in each year until this bond matures. Both principal and interest of this bond are payable in lawful money of the United States of America at the office of the Village Treasurer.

This bond is registered on the books of the village clerk and is transferable only upon presentation to such clerk with a written assignment duly acknowledged or proved. Upon presentation of this bond with such an assignment the clerk will note such transfer on this bond and on said books.

This bond is one of an issue of $10,000 bonds of like date and tenor, except as to denomination and maturity, numbered from 1 to 10 inclusive, issued pursuant to the provisions of the Village Law, constituting Chapter 64 of the Consolidated Laws of the State of New York, and a proposition duly adopted at an election held in said village November 8, 1921, and a resolution of the Board of Trustees of said village adopted November 10, 1921.

It is hereby certified and recited that all conditions, acts and things required by the constitution and statutes of the State of New York to exist, to have happened and to be performed precedent to and in the issuance of this bond, exist, have happened and have been performed, and that the issue of bonds of which this is one, together with all other indebtedness of said village, is within every debt and other limit prescribed by the constitution and laws of said state.

IN WITNESS WHEREOF, the village of Suffern has caused this bond to be signed by its President and its Village Treasurer, and the corporate seal of said Village to be hereunto affixed and attested by its Village Clerk this first day of December, 1921.

President
Village Treasurer

ATTEST:
Village Clerk
(Corporate Seal)

Form for Registration

This bond is registered as follows:

Date of Registry	Name of Registered Owner	Village Clerk

Chapter III

MUNICIPAL CORPORATIONS

Definition.—A corporation is a legal person, perfectly distinct from the members which compose it, having a special name and having such powers and such only, as the law prescribes. As Lord Coke says, it is "invisible, immortal, having no conscience or soul." A corporation can sue and be sued, have a common seal and have a continuous legal existence. A municipal corporation consists of the inhabitants of a given area constituted by the sovereign a body politic and corporate for the purposes of local government. Essentially its corporate character or *virtus* does not differ from that of a corporation as usually defined. The difference is in the powers granted by charter. And we hear so much of civic righteousness and civic conscience that we are constrained to think municipal corporations must have a soul.

A municipality is a creature of the State or sovereign. As Governor Miller said in an address to a delegation of New York City business men on March 15, 1921:

> There has been a good deal of talk about home rule with respect to this and other subjects and it has been made a sort of a fetish to cover misrule and misgovernment, and the people who are talking of it with respect to the municipalities of the State are looking at it from an entirely wrong angle.
>
> The municipalities have been created by the State. They are the mere creatures of the State as agencies for local administration, and their justification or excuse for the exercise of power stops at the point where they cease to be able effectively and efficiently to handle the problems.
>
> The welfare of the entire State is intimately bound up in the welfare of the City of New York. Now, the State has a responsibility which it cannot shirk. I believe in the very greatest measure possible for local self-government, and by that I mean of municipal local self-government, and by "possible" I mean the greatest measure that is compatible with good government; but the purpose of these municipal governments is to administer their functions in the interest of the people, and when they cease to be able to do that in reference to any given matter they cease to have any case whatever to support an argument for home rule, in my judgment.[1]

Municipalities subject to legislature of State.—These organizations are, of course, subject to the legislature of the

[1] *New York Evening Post,* March 15, 1921.

State, and their acts, if they violate the law or affect private rights, are also subject to judicial cognizance and judgment. They are under the law and are bound to obey it. While the community is entitled to local government, it cannot claim, as against the State, any particular charter or form of local government.

The constitution of each State contains provisions intended to make clear the principle of legislative control of municipalities, and to limit legislative interference. Thus in the constitution of New York State we find:

"It shall be the duty of the legislature to provide for the organization of cities and incorporated villages";[2] and "Corporations may be formed under general laws; but shall not be created by special act, *except for municipal purposes,* and in cases where, in the judgment of the legislature, the objects of the corporation cannot be attained under general laws. All general laws and special acts passed pursuant to this section may be altered from time to time or repealed."[3]

The reservation of power in this last sentence was rendered necessary by the Dartmouth College case[4] and is found in practically all, if not all, State constitutions.

The legislature of New York, pursuant to the mandate to "provide for the organization of cities and incorporated villages," has provided uniform charters for second-class cities[5] (in such a defective way that each second-class city has been obliged to obtain a supplementary charter), villages,[6] and towns.[7]

The constitution of New Jersey directs the legislature to provide general laws to regulate "the internal affairs of towns, and counties"; and prohibits the passage of private, local or special laws.[8] Town by judicial construction includes cities, boroughs and villages. Despite the prohibition, special acts are numerous, masquerading as general laws, and "ripper" bills mark each legislative session.

It is one of the fundamental principles of constitutional government that the legislature of a State cannot delegate the

[2] Art. XII, Sec. 1.
[3] Art. VIII, Sec. 1.
[4] *Dartmouth College v. Woodward,* 4 Wheat. (U. S.) 518.
[5] Cons. Laws, Chap. 53.
[6] Cons. Laws, Chap. 64.
[7] Cons. Laws, Chap. 62.
[8] Art. IV, Sec. VII, sub. 2.

power to make laws, which has been entrusted to it by the people, but the creation of municipalities exercising local self-government has never been held to trench upon that rule.

Creation of municipalities.—Municipalities may be created by special charter, which are their "articles of incorporation," stating the name, defining the territorial limits, limiting the electorate and granting powers of government. Such charter may be and frequently is amended, altered or repealed. For an example of what is ordinarily known as a "scissors and paste charter," the reader is referred to that remarkable document known as the Charter of the City of Cohoes,[9] the fiscal provisions of which are about as clear as the narrative of the Mormon bible.

Municipalities may be created pursuant to general laws. Thus in New York State a number of people, living in a limited area, may, by taking proper proceedings, form a village,[10] and in many jurisdictions cities may be so formed.

In New Jersey, boroughs (resembling villages in most States) are ordinarily incorporated, or chartered, by the legislature. The statute gives a name and defines the boundaries of the borough, which then becomes subject to and obtains its grant of powers from the Borough Law [11] and the Act concerning Municipalities.[12]

Many jurisdictions have codes or general statutes applying to all municipalities or all of a certain class, such as all cities in New Jersey and in New York.[13]

In England, though not in this country, a municipal corporation may be such by prescription—that is, its corporate powers have been exercised so long that a charter is supposed to exist and it is assumed that it has been lost. Defacto corporations result when proceedings to incorporate under a general law have been defective. The State only can attack the validity of such incorporation.

To sum up, we find that municipal corporations are created or come into existence by:

Special charter or
Incorporation under general laws;

[9] P. L. 1915, p. 353.
[10] Cons. Laws, Chap. 64.
[11] P. L. 1897, p. 285.
[12] P. L. 1917, p. 319.
[13] P. L. 1917, p. 319; Cons. Laws, Chap. 21, 53.

Prescription; and, through a failure properly to incorporate, a

Defacto municipal corporation.

Powers and functions of municipal corporations.—A municipal corporation possesses and can exercise the following powers and no others. First, those granted in express words; second, those necessarily or fairly implied in or incident to the powers expressly granted; third, those essential to the accomplishment of the declared objects and purposes of the corporation—not simply convenient, but indispensable. Any fair, reasonable, substantial doubt concerning the existence of power is resolved against the corporation, and the power is denied. These principles are of transcendent importance and lie at the foundation of the law of municipal corporations. An essential power would seem to be implied, if not expressly granted, so we may say that the powers of a municipal corporation are:

(a) Express—as the power to govern through specified officers and agents, and

(b) Implied—as the power to acquire a city hall or place to house such officers and agents must be, if not expressly granted.

Within the scope of our topic, we may illustrate by saying that the power to construct or acquire a water system is (almost always as to cities) expressly granted, and to pay for such system the power to borrow money may be implied, if not expressly granted. We will find later that power to borrow, whether expressed or implied, does not, according to the weight of authority, carry with it the power to issue or "emit" negotiable instruments, which, as we have seen, possess certain very interesting characteristics.

The essential branches of the power of the State which may be expressly granted by legislation to the municipality are:

(1) The police power, which does not mean alone the power of uniformed policemen but includes the right to make regulations necessary to the health, safety, welfare and comfort of the community;

(2) The power of taxation, with which we are directly concerned and which need not be further defined at this time; and

(3) The power of eminent domain, which in brief means

the right (by appropriate legal proceedings) to take private property such as land, for public purposes such as parks, upon making proper compensation to the owner.

Many if not all of such powers may be exercised by a municipal corporation in one of two different capacities, that is

(a) Governmental, legislative or public, or
(b) Proprietary or private.

The distinction is not easy to define and it will answer our purpose to say that governmental powers are political, to be exercised for the public good on behalf of the State, such as the power to maintain order and the public peace; and that proprietary powers are similar to those exercised by a business corporation over its property, such as the right to collect payment for water sold consumers, or to operate any public utility.

Classification.—The term municipal corporation is general and is not always accurately applied. The legislature may call a county a municipal corporation as in New York [14] or a "body politic and corporate" as in New Jersey.[15] Generally speaking, we mean all municipal or quasi municipal bodies, or even school or taxing districts. These have various names, broadly and usually not accurately descriptive of their functions:

(a) Counties are in a class by themselves as they are in reality major political subdivisions of the State. They are not in all States corporations, but the distinction between them and municipal corporations is mainly of governmental and historical significance.

(b) True municipal corporations, possessing in greater or lesser degree all the functions of local government and all the attributes of municipal corporations, are:

Cities, and sometimes
Towns,
Townships,
Villages and
Boroughs.

(c) Quasi municipal corporations, best described as local taxing districts with administrative powers presumably adequate for the purpose for which they are created, are:

[14] Cons. Laws, Chap. 24.
[15] An Act concerning counties, P. L. 1918, p. 567.

School districts.
Road, sewer, fire, etc., districts.
Drainage, irrigation or levee districts.

Frequently, if not always, the districts classified as quasi municipal corporations are co-extensive or practically so, or are included within true municipal corporations. A city may be and frequently is a school district and in it, overlapping each other, may be park, sewer and other taxing areas, or quasi municipal corporations. The consequences of this overlapping will be considered hereafter.

The distinction between municipalities is of importance in determining the valuation of securities, and is considered further in other chapters.

Chapter IV

MUNICIPAL PROPERTY AND IMPROVEMENTS

The history of the human race is the history of its cities. —Earliest recorded history is not only an account of wars and conquests; it is a record of co-operative undertakings. When we contemplate the pyramids and temples of Egypt, we are lost in admiration of their extent and magnificence and the human endeavor necessary to create such works. Our admiration may be qualified by a knowledge that the workmen were slaves and that the money was wrung from a peasantry by absolute monarchs. Yet there is a co-operation discernible, even if enforced.

We think of the Romans as road builders. Wherever Roman civilization extended, the paved causeway led from Rome to the outposts of that civilization. Bridges were necessary incidents. It is an interesting comment in passing that the spiritual head of the visible church takes one of his titles from the historic function of bridge building. The Pontifex Maximus was an important official of Ancient Rome and the Popes have succeeded to that title.

Hebrew history recalls the common endeavor headed by Sanballat to rebuild the shattered walls of Jerusalem after the captivity. There is, however, no evidence that the Jewish money lenders dealt in municipal bonds issued to provide funds for the purpose.

As civilization advanced, as human beings congregated, pure and plentiful water was found to be a necessity. Thence arose great systems of aqueducts. One with which we are all familiar, under the name of the Pont du Garde, crosses the Pontine Marshes to Rome. The great sewer supplementing the Tiber, known as the Cloaca Maxima, and the public baths, objects of daily resort of the aristocrat as well as the plebeian, still remain the wonder of the tourist.

With the spread of Christianity, necessarily came the thought of responsibility for others. Hence arose, growing

out of the monastic institutions, hospitals for the sick and asylums for the mentally and physically incompetent.

It is interesting (though not important) to observe that what the individual once did for himself, the municipality is now doing for him. The nearest lake or river provided a bathing place for primitive man. The Romans understood the necessity for public baths and provided them. After a hiatus in personal cleanliness for many centuries, the modern city erects public baths, and every residence is provided with more or less adequate facilities for bathing. Co-operation makes possible any number of things which the unaided individual would have difficulty in obtaining. So the public demand for improvements is each year carrying our municipalities farther along the road to socialism.

Municipal expenditures.—A municipality may expend its money only for a public purpose. What is a public purpose may not always be easy to determine but when determined it constitutes the limits of the power of taxation. The State legislature can neither compel nor authorize a municipal corporation to expend any of its funds for a private purpose and consequently, since practically every undertaking of a municipality does or may require the expenditure of money, a municipal corporation cannot, even with express legislative sanction, embark on any private enterprise or assume any function which is not public in a legal sense. If a specific provision prohibiting the expenditure of public funds for private purposes is required, it is found in the clauses of most State constitutions which forbid the taking of property for other than public uses; for since the funds of a municipality are necessarily directly or indirectly raised by taxation, the expenditure of money by a municipality for private purposes does or may necessarily result in the taking of property under the guise of taxation for other than public uses. It can make no difference that the payment is to be made out of borrowed money and that no immediate provision for taxation is made.

But the power of a municipality under legislative authority to expend funds raised by taxation upon public institutions, such as hospitals and schools which are owned, operated and controlled by the municipality, is unquestioned. Subject to constitutional restrictions, it is within the power of the legislature of a State to ascertain how the public burdens are to be borne.

As to what constitutes a public or municipal purpose (the terms are not necessarily synonymous) the decisions of the courts and the statutes are not uniform. It must, however, be for the benefit and use of the municipality itself. More specifically it has been said that a municipal purpose must concern primarily the benefit, use, or convenience of a municipality as distinguished from that of the public outside of it, and that it must be within the ordinary range of municipal action.[1]

Municipal expenditures are of two kinds: first, for running expenses; and second, for capital expenditures.

Running expenses.—By running expenses is meant expenditures for salaries, maintenance of property, cleaning streets, and the numerous duties which must continually be performed to keep the city moving.

Capital expenditures.—When property is to be acquired, or a building constructed, the expenditure of money is a capital expense. The entire cost of such a project can be met with money raised by taxation in one or more years. But it is advisable, if the amount of money needed be large, to spread the expense over a period of years. Therefore, the funds to pay for property acquired for public purposes or public improvements are frequently borrowed. This may be necessary because the amount required is too great to be included in the annual budget and raised by tax in one year. A municipality whose annual running expenses are half a million dollars may, and frequently does, construct a water or sewer system costing four or five times that amount. The effect upon the tax rate if the larger sum should be included in the budget can be imagined and has been explained in Chapter I. As we have seen, when money is borrowed for a capital expenditure, it is secured by the issue and sale of bonds.

Debt service.—Because of its importance, the author suggests debt service as a third division in the classification of municipal expenditures. By debt service, and it is a term we will frequently use, we mean the amount of money necessary each year to pay the interest on the public debt and to provide a fund for its redemption. This latter is usually the contribution to the sinking fund, but modern financing requires that funded debt be paid in annual installments, and in the debt

[1] *In re Mayor,* etc. (1885), 99 N. Y., 569 at 590.

service must be included the amount necessary to retire maturing obligations.

All municipal expenditures are made by the municipality in one of its two capacities, governmental or proprietary, but the distinction is not important in this discussion.

Acquisition of property.—By the immemorial usage of the country, it appears to be recognized that as an incident to the corporate powers of municipal corporations, they may purchase and hold property both real and personal. So also a municipal corporation has implied power to receive a gift of real estate for corporate purposes. As all corporations in this country are created by the legislature, they have only such powers as the legislature expressly confers and such as are necessarily or fairly incident thereto.

The same doctrine applies to and measures the corporate capacity to receive all property. In the absence of express prohibitory statutes which in terms confer and limit, and therefore define and measure the power, the capacity to acquire and hold property (real and personal) must be fairly incidental to some power expressly granted and absolutely indispensable to the declared purposes of the corporation. Any greater right than this is not only not granted but is impliedly denied.[2]

Sound as these observations are, the principle is not always practically important because in many jurisdictions statutory grants of power are so large and so all-embracing that there is practically no limit to the power to acquire and hold property and construct improvements, except that the exercise of such power must be for a public purpose; and the courts are gradually extending the meaning of "public purposes."

Methods of acquisition.—A municipal corporation acquires its property by purchase, by gift and by condemnation. These powers are usually conferred by express statute, that is either contained in the charter or exists in some enactment applicable to all municipalities of a certain class.

Purchase and gift need no explanation.

The power to condemn is the right to take private property on making to the owner compensation in the prescribed amount, for a designated municipal or public purpose.

Limitations.—There are limitations on the exercise of such grants of power, besides the limitation that the power must

[2] Dillon, p. 1556.

be exercised for public purposes. It is frequently required by statute that before a certain thing be done, the question of doing it must be submitted to a popular vote, or that if by ordinance or resolution the thing is directed to be done, a certain number of taxpaying electors may require a referendum. These limitations, however, are not so much limitations on the power as on the right to exercise or method of exercising the power.

Public Improvements.—The power of a municipality to undertake public improvements is subject to the same qualifications as its power to acquire public property. Its power to expend funds raised by taxation for works of internal improvement that are located within its limits and constructed and controlled by its own officials is unquestioned. It may expend its funds in works of external improvement, if of a public character, and subject to legislative regulation and control.

Statutory powers (Act concerning Municipalities in New Jersey).—The statutory powers of municipal corporations have been so greatly enlarged during the last few years, especially in New Jersey and to a hardly less extent in New York, that a discussion of general principles is a discussion of particular statutes. One of the best examples of such statutory grants is the Act concerning Municipalities in New Jersey.[3]

There is no power to acquire property or construct improvements which a municipality in New Jersey ought properly to have that is not granted by this statute. It is one of the best examples of codification and one of the best drafted statutes which we have, both in form and content. It must be read, as to the creation of funded debt, in connection with what is called the Pierson Bond Act.[4] Given the power to construct or acquire property or improvements by the Act Concerning Municipalities, the power to issue bonds is conferred by the Pierson Act.

Second Class Cities Law in New York.—In New York a good example is the Second Class Cities Law which gives such cities the right to create a funded debt for any municipal purpose, but it leaves to other statutes and to some extent to general principles the determination of the question, "What is a municipal purpose?" The Village Law is an example of

[3] P. L. 1917, Chap. 152.
[4] P. L. 1917, Chap. 240.

a statute giving somewhat limited powers and attempting to grant only such powers as should be exercised by a municipal corporation of that particular class.

General rights of municipalities.—In general, municipalities have the right to construct public buildings even without express legislative authority and to provide a meeting place for the voters of the municipality if it is a pure democracy, such as a New England town, or for the municipal council if it has a representative form of government; in other words, it has the right to build a city or town hall. Express legislative authority is, however, ordinarily found.

Municipalities almost invariably are granted the power of extending, improving, and grading streets and highways within their respective limits. It has been held that power to grade and improve its streets is an inherent corporate power. The construction of sewers and drains is a public and governmental function, and a municipal corporation may be required by the legislature to pay the cost of a sewerage system constructed without its consent.

A water supply is, of course, the most important requisite in a community of any size. The power of a municipal corporation, with legislative authority, to engage in the sale and distribution to its inhabitants for compensation, of a commodity which is essential to wholesome, comfortable and convenient living is well established, even if the business which is undertaken is one which can be, and ordinarily is, carried on by private capital. If it is an undertaking which cannot be carried on without the aid of some governmental franchise, such as the right of eminent domain, or the privilege of using the public streets for pipes and conduits, the appropriation of real estate for a water works may be authorized. In passing, we note that while there is no other distinction between water works operated by gravity and water works requiring pumping, the practical difference is important because of the small cost of operation of the former and the greater cost of operation of the latter.

Other activities.—Municipalities may acquire and maintain public lighting plants and engage in the business of supplying light and electricity. They may be expressly authorized by statute to erect public wharves and charge tolls for their use. The acquisition of parks and public places has long been recognized as a municipal function. Markets may be

acquired and constructed, and libraries built and operated but in this latter case the statutory power must be closely scanned.

While education is a function of the State and is generally recognized as such, the State, through the legislature, may impose upon the municipality the burden of constructing, operating and maintaining schools. It is to some extent the result of this theory that our public educational system is as good as it is, but out of the theory rises the extremely complex economic and political situation which we see illustrated by controversies between bodies with budget-making powers and boards of education.

Municipalities may make improvements and expend their funds for works of a public character even if these works are not wholly within the territorial limits of the municipality, provided they are connected with municipal improvements.

A city may be granted power to expend its funds in improving the navigation of a river upon which the municipality is situated, and we are familiar with the fact that the water supply of the City of New York extends northward through many cities and suburban communities to points geographically far removed from the city hall. There can be no doubt of the power of the legislature to authorize a municipal corporation to acquire the ownership of property outside its territorial limits, but this power must be expressly granted.

Public utilities.—The ownership and operation of public utilities is a large subject upon which we need spend little time. It may be and frequently is a political issue. It should be noted that there is an important distinction between public ownership and public operation but in either event the power must come from the legislature and be clearly granted in express terms.

Railroad aid as such is now fortunately forbidden by constitution and by statute, the enactment of such prohibitions resulting in most States from the abuses which occurred in the days of development and expansion following the Civil War. The power to own and operate street railroads is frequently given; for an illustration see the New Jersey Act concerning Municipalities. The exercise of such power is ordinarily made dependent upon a referendum of the taxpaying electors.

Sale of commodities.—It does not often happen that municipalities desire to function as retail merchants but we all

recall extensive operations of this character during the Great War. Most of such enterprises, namely the sale of government food products for the purpose of keeping down retail prices, were probably without authority of law, unless in some States statutes were hurriedly passed to permit the use of public places and public funds, and the participation of public officials. Most authorities agree that a municipal corporation cannot constitutionally be authorized by the legislature to engage in the business of selling and distributing the conveniences or even the necessities of life if the business is of such a nature that it can be carried on by private individuals without the aid of any franchises from the State.[5]

Building houses.—The housing situation existing in the years 1919 and 1920 in the Eastern States created a demand that municipalities engage in the business of building houses. This, it is safe to say, they cannot do without express legislative authority and it is very questionable whether such legislative authority can constitutionally be given.

In conclusion we may say: While the right of a municipality to acquire property and construct improvements may in some cases be inferred, the power is ordinarily given by express grant from the legislature. When the purpose for which a bond is issued appears to be unusual, for example to acquire a municipal graveyard, the statutes must be closely scanned. If the grant of power cannot be found, the inference must be extremely clear that such power exists or the doubt must be resolved against the existence. Practically, we find grants of power sufficient for proper municipal functions, according to their kind.

[5] 19 R. C. L., p. 719.

Chapter V

TAXATION AND LIMITATION OF TAXES

Municipal bonds redeemed by taxation.—Municipal bonds, with relatively unimportant exceptions, are redeemed with money raised by one form or another of tax. Taxation is, therefore, one of the most important of the subjects with which we shall have to deal.

Taxes defined.—Taxes, including assessments, are burdens or charges imposed either directly by the legislature, or under its authority, upon persons and property to raise money for public as distinguished from private purposes, or to accomplish some thing or object public in its nature. A public use or purpose is the *raison d'etre* of a tax. The substantial foundation of the power is political, civil, or governmental necessity, and taxes are largely if not wholly sacrifices for the public good. A tax may also be defined as an enforced contribution of money or other property, assessed, in accordance with some reasonable rule of apportionment, by authority of a sovereign State, on persons or property within its jurisdiction, for the purpose of defraying the public expenses. A tax is an obligation imposed upon citizens to pay the expenses of government and is in no way dependent upon the will or contract—express or implied—of the persons taxed.

Taxation is the principal source of revenue by which municipal expenses are borne and debts and liabilities paid. The primary form of tax in almost all of the States is the direct property tax levied at a uniform rate upon all the property, real or personal, within each city, town, or other civil unit or taxing district, and it is usually intended to reach all property taxable within the power of the State.

The power to tax.—The power to tax is inherent in the sovereign, which for our purpose is the State. The power of the States and of their municipalities to levy taxes is subject to certain express and implied restrictions under the Federal Constitution. It is sufficient to say that the only restriction of interest is the provision that States shall not pass laws impair-

ing the obligation of contracts. This is held to be a limitation upon the taxing power of the State. The right to tax is not granted by the constitution of a State, but of necessity underlies it because a government could not exist or perform its functions without it. While it may be regulated and limited by the constitution, it exists without express grant in words, as a necessary attribute of sovereignty. The provisions of the State constitutions, which relate to the power of taxation, do not operate as grants of the power of taxation to the governments thus set up but constitute limitations upon a power which would otherwise be without limit.

The power to tax is exercised by the legislature either directly through the passage of laws for the raising of revenues for support of the commonwealth, or indirectly by delegation to the municipalities or local taxing boards. Subject to constitutional restrictions, it is within the power of the legislature of a State to ascertain the public burdens to be borne and the persons or classes of persons who ought to bear them and its determination, within the limits of the constitution, is not judicially reviewable. Stated somewhat differently, we may say that the work of deciding what money shall be raised by taxation and what properties or privileges or occupations shall be taxed rests exclusively with the legislature without any limitations except such as are imposed by express constitutional provisions.

"The power of taxation being legislative, all the incidents are within the control of the legislature. The purposes for which a tax should be levied; the extent of taxation; the apportionment of the tax; upon what property or class of persons the tax shall operate; whether the tax shall be general or limited to a particular locality; and in the latter case, the fixing of a district of assessment; the method of collection, and whether the tax shall be a charge upon both person and property, or only on the land, are matters within the discretion of the legislature and in respect to which its determination is final." [1]

A municipal corporation established by the legislature cannot exercise the power of taxation without legislative authority. This is subject to the qualification that the authority of a municipality to tax is sometimes implied. For example, if the power to issue securities is given by statute, it

[1] *Genet v. City of Brooklyn* (1885), 99 N. Y. 296 at 306.

has been held by the United States Supreme Court that the power to tax to obtain funds to pay the interest and principal of maturing bonds may be implied.[2] That court has declared that if a municipal corporation is authorized to issue bonds it must levy a tax therefor unless the power be plainly and unmistakably negatived by the statutes authorizing the bonds; that is, it must exist by unmistakable implication.[3] It cannot be collected by doubtful inferences from other powers or powers relating to other subjects nor can it be deduced from any consideration of convenience or advantage.

Delegation of power.—The legislative branch of the government may delegate the power to tax to municipal corporations, but the power to tax cannot be delegated except for public purposes. In the absence of a constitutional restriction, the legislature may confer the taxing power upon municipalities in such measure as it deems expedient, in other words, with such limitations as it sees fit as to the rate of taxation, the public purposes for which the taxation is authorized, and the objects (the persons, business and property) which shall be subject to taxation.

It is well settled in most jurisdictions that the taxing power may be delegated to a district having very embryonic or no governmental functions, such as an irrigation, fire, or sewer district. This is true in most States but it is not true in New Jersey because of the constitutional restriction discussed in the Passaic Valley Sewer Case.[4]

"Public purpose" the boundary of taxation.—Taxes may be levied only for a public purpose. The definition of a public use or purpose is not easy. It has been defined in New York as follows: "The terms 'public or municipal purpose' and 'general welfare,' as used in this article, shall each include the promotion of education, art, beauty, charity, amusement, recreation, health, safety, comfort and convenience," etc.[5]

If a public purpose is not always easy to determine, it constitutes, when determined, the boundary of the power of taxation. As stated above, a public use or purpose is the essence of a tax. It is a well settled principle of constitutional law that no tax can be levied except for the purpose

[2] Dillon, p. 2398.

[3] *United States v. New Orleans* (1878), 98 U. S. 381; *Ralls County v. United States* (1881), 105 U. S. 733.

[4] *Van Cleve v. Passaic Valley,* etc. (1905), 71 N. J. L. 574; 60 Atl. 214.

[5] Cons. Laws, Chap. 31.

of raising money which is to be expended for the public use. To justify any exercise of the taxing power, the expenditure which it is intended to meet must be for some public service or some object which concerns the public welfare. This principle is fundamental and underlies all government that is based on reason rather than force.

It is said that levying a tax for a purpose not public is most obviously objectionable as it is taking the property of the person assessed without due process of law. Since such a burden is not a tax, to impose it is a mere spoliation of the individual without the sanction of any of the precedents which constitute due process of law. The application of the principle that taxes can be levied only for the public use extends far beyond the mere denial of the right to collect a tax which has been levied for a private purpose. The right to tax depends upon the ultimate use, purpose and object for which the fund is raised. This principle may accordingly be invoked by a taxpayer to prevent the expenditure of funds which have been or are to be raised by taxation for purposes not public and is a weapon which may be used to advantage.

If taxes cannot be *imposed* for a certain purpose, money already in the treasury cannot be *appropriated* for that purpose, and if taxes cannot be levied, bonds cannot ordinarily be issued.

A test of the right of taxation.—Perhaps the best test of the right of taxation is to ask whether the proceeds of the tax are to be used for the support of government or for some of the recognized objects of government, or directly to promote the welfare of the community. A purpose from the attainment of which will flow some benefit or convenience to the public is a public use.[6]

Classification of taxes.—Taxes have been classified by text writers as follows:

(a) Capitation or poll.

(b) Property, in which are included general taxes and assessments.

(c) Excise.

(d) Income.

Poll taxes.—A capitation or poll tax is one of a fixed amount operating upon all persons, or all persons of a certain class, resident within a specified territory, without regard to

[6] 26 R. C. L., p. 46.

their property or the occupation in which they may be engaged.

Property tax.—A property tax is the form most familiar to us and is ordinarily reckoned on the amount of property owned by the taxpayer on a given day and not on the total amount owned by him during the year, and it is ordinarily assessed at stated periods determined in advance and collected at appointed times. A tax computed upon the valuation of property, such as the value of one's dwelling, is considered a property tax.

A general property tax is laid on all the property, or all the property of a certain class, located within a specified territory, for the purpose of defraying the public expenses of that territory. Such a tax is based upon the theory that a certain amount of money must be raised to maintain the municipal government.

A special assessment, on the other hand, is laid upon property specially benefited by a local improvement in proportion to the benefit, for the purpose of defraying the cost of the improvement. It proceeds upon the theory that when a local improvement enhances the value of neighbouring property, it is reasonable and just for the legislature to provide that such property shall pay for the improvement. In a general levy of taxes, the contribution is exacted in return for the general benefits of government; in special assessments, the contribution is exacted because the property of a taxpayer is considered by the legislature to be benefited over and beyond the general benefit to the community. We find special assessments frequently levied for such improvements as grading and paving streets and sidewalks, constructing drains, sewers, and the like.

Excises.—An excise has come to mean every form of taxation which is not a burden laid directly upon persons or property, including every form or charge imposed by public authority for the purpose of raising revenue, upon the performance of an act, the enjoyment of a privilege, or the engaging in an occupation.[7] A chauffeur's license fee is a familiar illustration, as it is imposed directly by the legislature without assessment.

Income taxes.—Income taxes are of importance to the investor, as we shall see later, but only as to the income

[7] 26 R. C. L., p. 34.

derived therefrom and not as supporting the bonds.[8] As municipal bonds are not supported by income taxes, except in States which apportion and return to the municipality a part of the tax raised within it, in which cases the support is indirect, nothing further need be said at this point.

Debt service.—The interest on bonds and the money to pay the maturing installments of principal, or to provide the annual contributions to a sinking fund, is raised by tax and is called "debt service." Such tax should be a direct, ad valorem, real property tax, for no other form of taxation is sufficient protection for the bondholder. The reason for this is that the principal source of revenue of all civil divisions is such a tax on real property. Assessed valuations of real property tend to increase from year to year and not to decrease or fluctuate. A marked decrease in valuations may be a danger signal, and its cause should be investigated. The amount of a direct real property tax can be quite accurately estimated in advance, as can the amount or percentage of the tax which will be collected. The amount of tax which can be collected from personal property, or derived from income or poll taxes, tends to fluctuate, is small in amount as compared with the real property tax, and is not a dependable source of municipal income.

Taxation clause generally provides for payment of principal and interest.—Most statutes authorizing the issue of bonds by municipalities provide for the raising by taxation of sufficient funds to pay the principal and annual interest on the bonds. In New York, for example, the General Municipal Law[9] provides that every ordinance or resolution providing for the issue of bonds shall provide for a sufficient tax to pay the interest and maturing principal. In New Jersey, the Pierson Budget Act[10] in section 12, sub-division f, makes it mandatory upon the municipality, county, or school district, to include within the budget appropriations for the year a sufficient amount to meet sinking fund requirements and to pay bonds falling due within such year—which amount, of course, includes requirements for interest. It may be said that very few statutes which authorize the issue of bonds fail to provide for a sufficient tax, and that where specific provision is

[8] Chapter on Taxation of Bonds.
[9] Cons. Laws, Chap. 24.
[10] P. L. 1917, p. 548.

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not made in the statute itself, adequate provision is usually made by general laws. There are, however, exceptions.

Taxation provisions important to bondholder.—The bondholder must consider to what extent the statutes have conferred upon or denied to the municipality the general powers of taxation; for the courts are powerless to grant a remedy when the laws fail to provide for a sufficient levy or when taxation is restricted to such an extent as to make it insufficient. The courts have not the power to levy or collect taxes but may simply issue writs for the performance of these duties and coerce the proper officials when they exist and are to be found.[11] The extent to which the taxing power must be and the extent to which it may be exercised are most important considerations in purchasing municipal bonds.[12] It is well, therefore, to know that bonds are supported by the full taxing power of the municipality without limitations or restrictions.

Limitation on taxes.—In New York State, there is no limit upon the tax for debt service. The constitution contains the following limitation:[13] "The amount hereafter to be raised by tax for county or State purposes, in any county containing a city of over one hundred thousand inhabitants, or in any such city of this State, in addition to providing for the principal and interest of existing debt, shall not in the aggregate exceed in any one year two per centum of the assessed valuation of the real and personal estate of such county or city, to be ascertained as prescribed in this section in respect to county or city debt." The clause "in addition to providing for the principal and interest of existing debt" is regarded as constantly in force and to relate to new debt as well as old debt. While there is a limitation on taxation for general purposes in cities of over one hundred thousand inhabitants, the limitation does not apply to debt service. There is no statutory limitation in New York on taxes for debt service. In New Jersey, there is no constitutional or statutory limitation on taxation for debt service.

The Smith One Per Cent Law.—In many other States, we find limitations on taxation for debt service, as in Ohio, contained in what is known as the Smith One Per Cent Law.

[11] Chamberlain, p. 189.
[12] Chamberlain, p. 187.
[13] Art. VIII, Sec. 10.

(Code: §5649.) Such limitations on taxation for the payment of funded debt in that State have been modified by the new Ohio Bond Law, effective January 1, 1922.

In an article by Raymond C. Atkinson of Western Reserve University, entitled: "The Effects of Tax Limitation in Ohio Cities," printed in the *National Municipal Review* for December, 1920, there is a very concise and illuminating discussion of the effect of the Smith One Per Cent Law. It is interesting to note that the supreme court of Ohio in 1916, according to Prof. Atkinson, "definitely declared that full provision for interest and debt retirement takes precedence over all other expenditures." This is the reverse of the general rule.

Prof. Atkinson states that in 1917 "if all cities had met the interest on their bonds and the entire cost of debt retirement from taxation, debt charges alone would have exceeded the total tax revenue of the 80 cities of Ohio by $180,000. * * * Cities were confronted with the alternative of refunding their bonds as they fell due or of borrowing money for running expenses. The large cities compromised by doing both. In that way immense floating debts were incurred which cities were utterly incapable of paying, and the legislature was forced to authorize the issuance of deficiency bonds."

The Gardner Act.—Some relief was afforded by the so-called Gardner Act, which allowed taxing districts by popular vote to place their interest and sinking fund charges outside the 15-mill limit, but the Gardner Act is only a makeshift remedy at best.

"Fifteen mills may seem an adequate provision for municipal revenue, but it must not be forgotten that the city is only one of several agencies of government among which the 15 mills is parcelled out. The apportionment of the tax rate is entrusted to a county budget commission consisting of the auditor, treasurer, and prosecuting attorney—all county officials. The requirements of the State are first provided for, and needless to say, the budget commissioners see that the county receives second consideration. The requests of the school board usually come next in the order of preference, while the city, library board and other agencies of government have to be content with what remains."

Argument against any tax limit.—That limitations on

taxation for general purposes are vicious, is to some extent a matter of debate. Among the arguments that may be urged against municipal tax limits are the following:

The object of a limit on taxation for current expenses is sufficiently provided for by the accountability of the municipal authorities to their constituents. In the event of the city government being extravagant the taxpayers have ample power to apply, and will apply, the necessary check by refusing to re-elect the members responsible for such extravagance. Owing to the difference of conditions in various cities, and owing to the fact that a situation may be created from time to time, which would make a limit that was proper for one year absolutely improper for another year, it is not practicable to fix upon a general tax limit for all cities. One of the results of limitations on taxation for current expenses is that municipalities issue long-term bonds for current expenses, in order to avoid the limitation. This evil exists even where the tax limit applies to bonds as well as to current expenses, because the taxation to pay the bonds is, of course, spread over a period of years.

In an article by Mr. H. G. Loeffler, appearing in the *National Municipal Review*, entitled, "Municipal Tax Limits and Economy," it is said: "Where limits prevail, one of three things happens. The cities bring pressure to bear until the limit is raised, or they resort to continued court action until a satisfactory decree is obtained from the judiciary, or they fund the amount needed over future years by bonding. It is certain that the elected officials will do all in their power to satisfy the growing demands of the public. Experience seems to indicate that heretofore they have been successful, laws notwithstanding.

"There is only one way out of this situation after tax limits are abolished. That way lies along the lines of an efficient budget system. Make this system a picture of the services demanded from the government. Center the responsibility for the administration of it in one single elected official. Place on the statute books a bonding act which will not allow the cities to follow an unsound borrowing policy such as is being forced on many of them now by tax limits and special bonding laws.

"It is felt that if a process such as this is worked out, limitations of tax levies will be uncalled for. The State laws

will not then be productive of vicious bonding. In the budget the public will see the result financially of any new or extended governmental service demanded. If they feel that this new activity is worth the cost, let them so decide. The power will then rest where it should and tax limits will be unnecessary."

Arguments against any tax limits on debt service.—The object of a tax limit applicable to municipalities is sufficiently provided for by a limit on the amount of bonds that may be issued. No limit should be placed on the power of the municipal debtor to pay its debt. It is immoral not to pay debts. A tax limit that applies to municipal bonds injuriously affects municipal credit and tends to make bonds unmarketable. If the whole of the tax that could be levied within the limitation should be needed to pay the principal and interest of bonds, and the assessed valuation of property should be reduced so that the tax would be insufficient to pay all the bonds, the holders of the bonds first issued would have no better rights than the holders of the last bonds issued. Bonds subject to a tax limit will not be accepted by the board of trustees of the Postal Savings system nor by some of the large insurance companies.

Revenue.—Taxes are not the only source from which municipalities derive funds. Moneys coming from any other sources such as water rents, surplus earnings (if any) from other public utilities, the municipal share of certain State taxes, which may be considerable in amount, are usually designated as "revenue." These are so uncertain and are relatively so unimportant that the bondholder is not especially concerned and the careful buyer of municipal securities will not attach much importance to them.

Chapter VI

MUNICIPAL BORROWING

The power to incur indebtedness.—Every business corporation has the privilege of borrowing money to carry out the powers granted to it in its charter. It does not follow that this is equally true of municipal corporations. The power is sometimes implied but is closely watched by the courts, and as it is apt to be subject to judicial review, the courts have had more opportunity to limit the power than in the case of the moneyed or business corporation.

The power to borrow is usually given in express language, in which case the terms and purposes of the grant will measure its extent. If the power is not expressly conferred, does it, asks Judge Dillon, exist by implication? "The question of the incidental authority of municipal corporations to borrow money has often been considered and often decided, but the decisions are not uniform or reconcileable as to the extent or even existence of such authority. In view of the legislative practice to confer, in terms, all powers so important as this, the dangerous nature of this power, by reason of the temptation it holds out to incur needless debts and to make extravagant expenditures, and the facilities it offers for frauds, and the settled and salutary doctrine that such corporations have no powers but such as are expressly conferred, and those which are necessary to effect the objects of the corporation, and those which are incidental to the express grants where the legislative will is wholly silent," Judge Dillon "is strongly inclined to deny the existence of a general implied or general incidental power to borrow money, or much less to issue negotiable paper." [1]

"The power to borrow money is, in a certain sense, a larger power than that of raising money by taxation. The resistance of the parties taxed is, in the nature of the thing, an immediate check to taxation, which does not exist in the case of a power to borrow, for the immediate burden of a

[1] Dillon, p. 522.

loan is but slightly felt. Therefore the power to borrow money should not be inferred from any of the ordinary powers conferred in the charters of municipal corporations, and under ordinary circumstances such a power can proceed only from an express grant to that effect." [2]

Summary of Judge Dillon's views.—The following is a summary of Judge Dillon's views: [3] Whether there is power in a municipal corporation to borrow money or to issue negotiable paper or to do both depends upon the legislative intent, to be collected from statutes, general and special, applicable to the municipality or to the particular case.

1. The power to borrow money as a means of raising a fund to make future local improvements or to carry on the ordinary operations of the municipality cannot be implied from the mere authority to make such improvements or from the general grants of municipal power. These usually contemplate that the expense of the execution of the ordinary municipal powers shall be met by the revenues derived each year from taxation. (It should be kept constantly in mind that annual taxation is the normal means of raising funds, and borrowing is abnormal.—*Author.*)

2. It does not follow, because banking, trading, and other private corporations organized for pecuniary profit are held in this country to possess the incidental power to borrow money and to issue commercial paper having all the qualities attributed to such paper by the Law Merchant, that a like power is inherently possessed by public and municipal corporations. The analogy is false and delusive. * * * The nature of the usual duties devolved by law upon municipalities does not make it necessary to imply the existence of a general power to borrow money and to issue commercial paper.

3. The power to issue commercial paper which is unimpeachable in the hands of the holder, is not among the ordinary incidental powers of a public or municipal corporation. It must be conferred expressly, or by fair implication, as a necessary, or at least a reasonable and usual, means of executing the particular power to which it is claimed to be incidental. * * * Any fair or substantial doubt on this point is fatal to the existence of such power.

4. Express power to borrow money, in some States

[2] Dillon, p. 532.
[3] Dillon, p. 539.

* * * will be taken, if there be nothing in the legislation to negative the inference, to include the power, * * * to issue negotiable paper with all the incidents of negotiability. But under * * * a constantly increasing weight of authority * * * an express power to borrow does not necessarily authorize the issuance of negotiable paper, the power to give to evidences of municipal indebtedness and municipal obligations the characteristics of negotiability being a power which must be conferred upon the municipality either in express words or their equivalent by necessary implication.

5. Although a municipal corporation * * * may * * * create debts, and may, when not restrained by statute, evidence the liabilities thus incurred, yet if the instrument is made to assume the form of negotiable paper, such paper is always open to defenses in the hands of the transferees when it is issued without express authority from the legislature, or authority clearly to be implied from the charter or legislation applicable to the municipality.

Stated in other words, Judge Dillon regards it as the true doctrine that, "merely as incidental to the discharge of its ordinary corporate functions, no municipal or public corporation has the right to invest any instrument it may issue, whatever its form, with that supreme and dangerous attribute of commercial paper which insulates the holder for value from defenses and equities which attach to its inception." [4]

Limitations on incurring indebtedness.—A limitation placed by law on municipal debt creation is generally assumed to be a protection to bondholders. The limit is usually a percentage of the assessed valuation of taxable real property. If it is too low it may hamper the city in obtaining needed capital for improvements.

The object of a limitation on indebtedness is obviously to prevent the increase of the burden of taxation or to keep taxation within limits which may be easily borne. It is generally based on real property valuations because these are more stable than taxes on personal property. Like all statutory limitations, the power is frequently evaded and many devices have been employed to evade the restrictions placed about the power to contract debts. Notable among these is the plan to provide municipal water works by purchasing a plant privately built, subject to the water bonds outstanding which, as they

[4] Dillon, pp. 539-543.

are not a direct municipal obligation, are not a part of the municipal debt.[5] As, however, the water bonds must be redeemed from the proceeds of taxation, direct or indirect, it seems that this evasion would not be successful. In general, it may be said that constitutional or statutory provisions in regard to the creation of local debt which are too strict or too narrow are undesirable and likely to lead to a long list of exceptions and special acts which, in the end, will take much of the effectiveness out of the limitations.[6]

Constitutional debt limits.—A constitutional debt limitation, while a protection to the bondholder, is a serious thing because bonds issued in violation of the limit are invalid. The bondholder may obtain relief from the disastrous effects of a statutory debt limit by an appeal to the legisature but there is no such appeal from the effect of a constitutional limitation.

"As long as the municipality has a sufficient margin within which it may incur debt for its ordinary purposes, no difficulty is met with in complying with the simplest and most absolute limitation; but the moment that the constitutional debt limit is reached or so closely approached that a city no longer has the credit which will enable it to finance its affairs, it is apparent that difficulties immediately arise. The city must continue to manage its affairs in some way. It must meet current expenses, and it may be that the health and well-being of the citizens imperatively require the expenditure of large amounts. The municipal officers try to overcome these difficulties as best they can, and out of their action litigation frequently follows. The nature of the difficulties which have arisen is reflected in the elaborate constitutional provisions which have been adopted in later years. Each qualification, restriction, or additional safeguard thus inserted has been adopted for the purpose of overcoming some difficulty or correcting some abuse which was found to exist under the simpler form of constitutional limitations, and each of these qualifications, restrictions, and additional safeguards practically represents some matter with which the courts have been obliged to deal." [7]

Excepted purposes.—Many State constitutions make provision for water and sewerage "by declaring that the debt

[5] Chamberlain, p. 224.
[6] Raymond, p. 152.
[7] Dillon, p. 341.

incurred for water supply or for sewers shall not be subject to the limitation, or by declaring that the debt limit may be increased for the purpose of purchasing or constructing water works or sewers; in some instances, lighting plants are placed upon a similar footing." [8] The reason for such exceptions is obvious. A pure and wholesome supply of water and the disposal of refuse matter are both imperative necessities in large communities. Indeed, there is another reason for the exemption of water debt, for where the water system operates by gravity and not by pumping, the revenues should be sufficient to maintain the plant and provide the necessary funds for debt service. Lighting plants are in many jurisdictions regarded, at least in theory, as self-sustaining public utilities. By "self-sustaining" is meant that the revenue or income from the utility is sufficient to pay operating charges and interest and principal of the debt incurred in its acquisition.

Illustrations.—To illustrate these statements, the constitutional and statutory limitations applying to New York State municipalities on incurring debt may be considered. Similar provisions are found in the constitutions and laws of many States.

"No county, city, town or village shall * * * be allowed to incur any indebtedness except for county, city, town or village purposes * * *. No county or city shall be allowed to become indebted for any purpose or in any manner to an amount which, including existing indebtedness, shall exceed ten per centum of the assessed valuation of the real estate of such county or city subject to taxation, as it appeared by the assessment rolls of said county or city on the last assessment for State or county taxes prior to the incurring of such indebtedness; and all indebtedness in excess of such limitation, except such as may now exist, shall be absolutely void, except as herein otherwise provided. No county or city whose present indebtedness exceeds ten per centum of the assessed valuation of its real estate subject to taxation shall be allowed to become indebted in any further amount until such indebtedness shall be reduced within such limit." [9]

Exceptions.—Exceptions in regard to indebtedness incurred in anticipation of the collection of taxes and applying

[8] Dillon, p. 339.

[9] Constitution, Art. VIII, Sec. 10, as last amended November 6, 1917, in effect January 1, 1918.

to the City of New York follow, and the section further provides:

"Nor shall this section be construed to prevent the issue of bonds to provide for the supply of water; but the term of the bonds issued to provide the supply of water, in excess of the limitation of indebtedness fixed herein, shall not exceed twenty years, and a sinking fund shall be created on the issuing of the said bonds for their redemption, by raising annually a sum which will produce an amount equal to the principal and interest of said bonds at their maturity. All certificates of indebtedness or revenue bonds issued in anticipation of the collection of taxes which are not retired within five years after their date of issue, and bonds issued to provide for the supply of water, and any debt hereafter incurred by any portion or part of a city, if there shall be any such debt, shall be included in ascertaining the power of the city to become otherwise indebted; except that * * * debts incurred by any city of the second class after the first day of January, nineteen hundred and eight, and debts incurred by any city of the third class after the first day of January, nineteen hundred and ten, to provide for the supply of water, shall not be so included."

Note that the constitutional limitations apply only to counties and cities, not to villages, towns or school districts. The limitations applying to the City of New York are omitted as being special in their application and not of general interest.

While these provisions are self-executing (that is, legislation is not necessary to make them workable), the same article and section of the constitution directs the legislature to "prescribe the method by which and the terms and conditions under which the amount of any debt to be so excluded shall be determined, and no such debt shall be excluded except in accordance with the determination so prescribed."

In the New York General Municipal Law, which applies to counties, towns, cities and villages, we find:

"No county containing a city of more than one hundred thousand inhabitants, nor any such city shall contract any debt, the amount of which, exclusive of its outstanding debt, shall exceed a sum equal to five per centum of the aggregate valuation of the real property within its bounds, as assessed for State and county purposes upon the then last corrected assessment-roll, nor shall it contract any such debt if the

amount thereof inclusive of its outstanding debts shall exceed a sum equal to ten per centum of such valuation. This section shall not be construed to prevent the issuing of certificates of indebtedness or revenue bonds issued in anticipation of the collection of taxes of amounts actually contained or to be contained in the taxes for the year when such certificates or revenue bonds are issued and payable out of such taxes. Nor shall this section be construed to prevent the issuing of bonds to provide for the supply of water, but the term of the bonds issued to provide for the supply of water shall not exceed twenty years, and the sinking fund shall be created on the issuing of said bonds for their redemption by raising annually a sum which will produce an amount equal to the amount of the principal of said sum and interest of said bonds at their maturity. This section shall not apply to debts contracted for the purpose of retiring or paying any existing indebtedness pursuant to the provisions of this chapter." [10]

The Village Law provides that:

"A village shall not incur indebtedness if thereby its total contract indebtedness, exclusive of liabilities for which taxes have already been levied and obligations issued to provide for the supply of water, shall exceed ten per centum of the assessed valuation of the real property of such village, subject to taxation, as it appeared on the last preceding village assessment-roll." [11]

Typical debt statements of second and third class cities in New York follow this chapter. They should be read in connection with the foregoing extracts from the constitution and statutes.

Debt limit contained in Pierson Act.—In the State of New Jersey there is no constitutional debt limit and the statutory limitation is, so far as is germane to our inquiry, contained in the Pierson Act.[12]

When Mr. Pierson and his collaborators began their work of drafting a uniform statute to govern the issue of municipal obligations, it was found necessary to limit in some way the indebtedness which might be incurred. The power of counties to incur debt is limited to four per cent of the average assessed valuation of the taxable real estate for the preceding

[10] Cons. Laws, Chap. 24, Sec. 3.
[11] Cons. Laws, Chap. 64, Sec. 130.
[12] P. L., 1917, p. 803.

three years. Municipal indebtedness other than that of counties is limited to seven per cent, although in certain cases additional indebtedness not to exceed two per cent may be incurred. The method of arriving at these percentages is highly artificial. It may have been, for example, that certain municipalities were largely indebted for the construction of bulkheads intended to protect the water front from encroachments by the sea, and if this debt were counted against the borrowing power, very little margin would remain. Hence it is provided that such debt may be excluded in its entirety. In cities (or other municipalities operating under the "City" article of the School Law) indebtedness incurred for educational purposes may be excluded, if it does not exceed three per cent of the average assessed valuation of the taxable real property for the preceding three years, or if it does, an amount equal to three per cent may be excluded. So, also, water bonds may be excluded in their entirety.

Typical annual and supplemental debt statements of a large New Jersey city filed pursuant to the statute follow this chapter; after which is a summary statement of the indebtedness of the same city at substantially the same time. The latter statement shows the true debt. The two former show the highly artificial deductions permitted by the statute. It is obvious that the net debt stated in this manner may be very far from reflecting the real condition of the municipality.

In conclusion it may be said that indebtedness of ten per cent is dangerously high.

The power to issue negotiable instruments.—As we have seen, the weight of authority is that municipal corporations have no implied power to issue negotiable instruments but such a power must be looked for in the charter or some other act of the legislature; "the legislative act, being the only source of the authority, measures and limits the power it confers." [13] If the statute gives no power to issue the bond, the municipality is not bound.[14] "A municipality can only act under and in accordance with the statutory authority which is conferred upon it. If the power is limited, it cannot exceed the prescribed limit, and its power is exhausted when the limit is reached. If it requires further powers, it must obtain

[13] Dillon, p. 1354.

[14] *U. S. v. Macon* (1878), 99 U. S. 582.

these by a further grant from the legislature. In granting such authority the power of the legislature is supreme, except in so far as it is limited and controlled by constitutional provisions." [15] The rule is that whenever the power to issue bonds is called in question, the authority to issue must be clearly shown and will not be inferred from uncertain data and can only be conferred by language which leaves no reasonable doubt of intent to confer it.[16]

This canon is so well recognized that express power, ordinarily sufficient to the needs of the municipal or quasi-municipal corporation, is usually found in charters or general statutes applicable to the municipality.

Power to issue bonds.—The power to issue negotiable long-time bonds is one which experience has shown to be especially liable to serious abuse. The proneness of municipalities to incur indebtedness, especially if its burden can be thrown upon posterity, is well known and needs, in the interest of the public welfare, to be regulated and restricted. Power to create debts payable in the future is necessary in order to enable municipalities to make expensive and permanent local improvements such as building sewers, paving streets, erecting necessary public buildings, procuring public parks, constructing or acquiring water works, lighting plants, and other public utilities if desired. The burden of such large expenditures should not be paid immediately but spread over a reasonable period of time.[17]

Illustrations of statutes granting bond-issuing power.—For illustrative statutes granting power to issue bonds, we may again turn to New York and New Jersey.

The statutory authority for the issue of bonds in New York is found in several general statutes and in many special ones. We need consider only the following:

The County Law.—The County Law provides that boards of supervisors may:

"Borrow money when they deem it necessary for the erection or alteration of county buildings and for the purchase of sites therefor, on the credit of the county, and for the funding of any debt of the county not represented by bonds, and issue county obligations therefor, and for other lawful

[15] Dillon, p. 1358.
[16] Dillon, p. 1359.
[17] Dillon, p. 336.

county uses and purposes; and authorize a town in their county to borrow money for town uses and purposes on its credit, and issue its obligations therefor, when, and in the manner, authorized by law." [18]

The General Municipal Law.—As pointed out above, the General Municipal Law applies to counties, towns, cities and villages. It also provides that:

"A funded debt shall not be contracted by a municipal corporation, except for a specific object, expressly stated in the ordinance or resolution proposing it; nor unless such ordinance or resolution shall be passed by a two-thirds vote of all the members elected to the board or council adopting it, or submitted to and approved by the electors of the town or county, or taxpayers of the village or city when required by law. * * * Such ordinance or resolution shall provide for raising annually, by tax, a sum sufficient to pay the interest and the principal, as the same shall become due." [19]

This statute also contains adequte provisions for the levy of a tax for debt service,[20] for refunding,[21] and registration,[22] and will repay study.

The General City Law contains a general grant of power for all cities:

"To become indebted for any public or municipal purpose and to issue therefor the obligations of the city, to determine upon the form and the terms and conditions thereof, and to pledge the faith and credit of the city for payment of principal and interest thereof, or to make the same payable out of a charge or lien upon specific properties or revenues; * * * To establish and maintain sinking funds for the liquidation of principal and interest of any indebtedness, and to provide for the refunding of any indebtedness other than certificates of indebtedness or revenue bonds issued in anticipation of the collection of taxes for amounts actually contained or to be contained in the taxes for the year when such certificates or revenue bonds are issued or in the taxes for the year next succeeding, and payable out of such taxes." [23]

This statute also provides that before bonds may be

[18] Cons. Laws, Chap. 11.
[19] *Id.*, Chap. 24, Sec. 6.
[20] *Id.*, Sec. 7.
[21] *Id.*, Sec. 8.
[22] *Id.*, Secs. 10, 11.
[23] *Id.*, Chap. 21, Sec. 20, sub. 5.

issued, a statement of the financial condition of the city must be made by the comptroller and filed in the office of the city clerk. Under well-established principles every purchaser of bonds is charged with notice of the contents of this certificate and an examination of a properly prepared certificate should show whether or not the city is within its debt limit. See the debt statement of a New York third class city, which follows this chapter. The provisions of the Second Class Cities Law [24] in regard to temporary and funded debts are very liberal and permit the creation of a funded debt "for any municipal purpose." This statute also contains various limitations upon the grant of power, as to maturities, execution, sale, and medium of payment, and the following interesting estoppel provision:

"An ordinance creating a funded debt may provide that the bonds therein authorized shall contain a recital that they are issued pursuant to law and an ordinance of the common council, as provided by section sixty of the Second Class Cities Law. Such recital, when so authorized, as aforesaid, shall be conclusive evidence of the regularity of the issue of said bonds and of their validity." [25]

The Pierson Act of New Jersey.—In New Jersey, the power to incur debt and issue negotiable instruments for municipal capital expenditures is found in the Pierson Act,[26] so frequently referred to. This act provides that any county or municipality shall have power to "borrow money and issue its negotiable bonds to pay for any improvement or property which it is or may be authorized or required by law to make or acquire, or for any other purpose which it is authorized or required by law to undertake or for which it is authorized or required by law to make an appropriation or to refund bonds * * * or for two or more such purposes." The machinery of issuing bonds under this statute is extremely interesting and will well repay examination in detail. Briefly, the term of the bonds depends upon the life of the improvements, as defined in the act. Valuable estoppel provisions and an extremely interesting scheme of public sale which will be examined later in more detail are also to be found.

[24] Cons. Laws, Chap. 53, Secs. 60, 61.
[25] *Id.*, Sec. 60.
[26] P. L. 1917, p. 803.

The Municipal Finance Act of North Carolina.—Probably one of the best illustrations of statutes authorizing the issue of bonds, limiting the power to issue them and prescribing the method of issue, is the Municipal Finance Act of North Carolina. It is so important that it is given in its entirety as an appendix to this volume, and will well repay careful study.

Refunding.—The power to refund valid and subsisting debt must ordinarily be expressly granted for the reason that the exercise of the power inevitably results in the issue of negotiable securities. Refunding does not increase the municipal debt. It merely changes the evidence of the debt and the time of its payment. If valid bonds have been issued and the municipality has exceeded its debt limit, maturing bonds may nevertheless be refunded (pursuant to proper statutory authority) in spite of the excess of indebtedness, for the reason that the refunding operation, as stated, does not increase the debt.

Legislative ratification.—In conclusion it may be noted that where municipal bonds are issued without proper authority, the legislature may legalize the unauthorized acts, provided it might have conferred authority before the unauthorized acts were committed,[27] but corporate ratification without legislative authority cannot make a municipal bond valid which was void when issued.[28]

Short term loans.—These are made in anticipation of the collection of taxes and to finance temporarily the construction cost of improvements. By temporary financing, the cost of an improvement may be determined in advance of a permanent bond issue, and an overissue avoided. For loans of this class, the economic basis is different from that for long term bonds. Such loans are highly regarded by many investment bankers and by banking houses generally, because they are more or less liquid assets, paid from the current taxes in anticipation of which the loans are made, or funded when permanent bonds are issued. Until recently, it was not the custom to require the opinion of counsel as to the legality of such loans but the practice is growing.

[27] *Anderson v. Santa Anna* (1885), 116 U. S. 356.
[28] *Lewis v. City of Shreveport* (1883), 108 U. S. 282.

Debt Statement of a New York Second Class City

Schedule No. 1

STATE OF NEW YORK }
COUNTY OF WESTCHESTER } SS:

I, JAMES W. HOWORTH, City Clerk of the City of Yonkers, do hereby certify that the assessed valuation of property subject to taxation located within the City of Yonkers in the year 1921, for the purpose of State, County and City, as shown by the assessment rolls for said year, is as follows:

Real Estate	$174,856,895.00
Personal	348,550.00
Special Franchise	3,266,142.00
	$178,471,587.00

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of the City of Yonkers, this 15th day of January, 1921.

J. W. HOWORTH,
City Clerk.

STATEMENT OF CONSTITUTIONAL DEBT-INCURRING CAPACITY OF THE CITY OF YONKERS, N. Y., AS OF FEBRUARY 10, 1921, INCLUDING $2,312,000.00 BONDS TO BE SOLD JANUARY 25th, 1921.

Limit:

Ten per centum (10%) of Assessed Valuation of Real Estate (including Special Franchises) as filed with the City Clerk, October 1, 1920, subject to taxation in 1921 (Schedule No. 1)	$17,812,303.70
Net Debt: (Schedule No. 2)	12,490,749.20
Margin of Debt-Incurring Capacity as of February 10th, 1921	$ 5,321,554.50

Schedule No. 2

DESIGNATION AND PURPOSE OF BONDS

City Hall	$ 275,800.00
Local Improvement	2,308,533.33
Deficiency	1,396,500.00
Building	200,050.00
Water	2,495,250.00
Equipment	186,800.00
Street Paving	109,280.00
Park	144,000 00
Street Repair	6,000.00
Road Improvement	81,500.00
School	3,852,810.00
Hospital	113,750.00
Assessment	1,511,000.00
Tax Sale	355,000.00
Grade Crossing Elimination	149,000.00
Dock	154,000.00
Total Bonds	$13,339,273.33

NOTES:		
Local Improvement	$ 1,409,000.00	
Bond Notes	1,238,000.00	
In anticipation of the collection of Taxes and Revenues	2,350,000.00	
Total Notes		$ 4,997,000.00
CONTRACT LIABILITY		861,476.08
LAND LIABILITY		20,000.00
Total Indebtedness		$19,217,749.41

DEDUCTIONS—TO ASCERTAIN MARGIN OF DEBT INCURRING CAPACITY

Notes maturing within five (5) years from date of original issue, in anticipation of taxes now outstanding	$ 1,828,851.60
Sinking Fund for Water Bonds issued prior to January 1, 1908	80,408.92
Water Bonds issued after January 1, 1908, to provide for the supply of water, less the amount thereof used to pay debts contracted for prior to January 1, 1908	1,435,250.00
Proceeds of Bonds and Notes to pay liabilities included above (not including proceeds of Water Bonds)	2,391,033.01
Outstanding Bonds maturing this year, provided for in annual estimate of 1921 (not including Bonds otherwise deducted)	991,456.67
TOTAL DEDUCTIONS	$ 6,727,000.20
NET DEBT	$12,490,749.20

STATE OF NEW YORK }
COUNTY OF WESTCHESTER } SS:

I, JAMES J. LYNCH, Comptroller of the City of Yonkers, State of New York, do hereby certify that the statements hereto annexed, concerning the finances of said city, are true and correct as appears from the records of my office.

IN WITNESS WHEREOF, I have hereunto set my hand this 15th day of January, 1921.

JAMES J. LYNCH,
Comptroller of the City of
Yonkers, New York.

Debt Statement of a New York Third Class City

STATE OF NEW YORK }
COUNTY OF ALBANY } SS:

Pursuant to Section 23-a of the General City Law constituting chapter 21 of the Consolidated Laws, I, the undersigned, Comptroller of the City of Cohoes, hereby certify:

(1) The existing indebtedness of the City of Cohoes, on the date of this Certificate is One million two hundred eighty-five thousand one hundred forty-two dollars ($1,285,142.00).

(2) The amount thereof consisting of bonds issued to provide for the supply of water issued prior to January 1, 1910, and also bonds issued thereafter to refund bonds issued prior to such date, or the term of which is more than twenty years in Two hundred forty-three thousand Dollars ($243,000).

(3) The amount thereof consisting of bonds issued to provide for the supply of water issued after January 1, 1910, except the refunding bonds specified in paragraph 2, the term of which is not more than twenty years is Seventy-three thousand Dollars ($73,000).

(4) The amount of sinking fund for the redemption of outstanding bonded indebtedness is (a) for the redemption of water bonds, nothing; and (b) for the redemption of other bonds, Six thousand six hundred seventy-four and 67/100 Dollars ($6,674.67).

(5) The amount of certificates of indebtedness or revenue bonds issued in anticipation of the collection of taxes outstanding (a) more than five years is nothing, and (b) less than five years is nothing.

(6) The amount of such certificates of indebtedness or revenue bonds which has not been paid out of taxes for the year when such certificates or revenue bonds were issued, or for the year next ensuing is nothing.

(7) The amount of the assessed valuation of the real estate of the City of Cohoes, subject to taxes shown by the assessment rolls of said City on the last previous assessment for State or County taxes is Twelve million sixty-three thousand two hundred sixty-seven Dollars ($12,063,267).

(8) A description of the property or improvement for the acquisition or making of which the debt is to be created and the probable life or such properties or improvements is (Omitted).

IN WITNESS WHEREOF I have hereunto set my hand at the City of Cohoes, New York, this 15th day of October, 1921.

City Comptroller.

Annual Debt Statement of a New Jersey City

STATE OF NEW JERSEY } SS.
COUNTY OF HUDSON }

James F. Gannon, Jr., being duly sworn deposes and says: Deponent is the Director of Revenue and Finance hereinafter called "the municipality" and the chief financial officer thereof. The Annual Debt Statement annexed hereto and hereby made a part hereof is a true statement of the debt condition of the municipality as of December 31, 1920. The amounts of such items as are indefinite or unascertainable are estimated.

JAMES F. GANNON, JR.

Subscribed and sworn to before me
this first day of January, 1921.

RICHARD ROE,

Notary Public of New Jersey.

A. GROSS INDEBTEDNESS

The gross indebtedness of the municipality, inclusive of notes or bonds authorized but not issued and obligations of the municipality held uncanceled in any sinking fund, exclusive of indebtedness incurred for current expenses of the current fiscal year and inclusive of notes and bonds and certificates of the municipality issued for school purposes other than for the current expenses of

schools, but not including the indebtedness of any school district constituting a separate corporation, is as follows:

(*a*) *Bonded Debt.* (*Including bonds authorized but not issued.*)	
1. Bonds payable or to be payable in whole or in part out of special assessments on property specially benefited	$ 3,179,004.95
2. Bonds issued, and authorized but not issued, for the following purposes so far as separately authorized or issued for such purposes:	
Docks	251,000.00
Water supply	14,650,254.72
Electric light or power	None
Gas	None
Markets	None
3. Bonds issued, and authorized but not issued, for other purposes from the carrying out of which the municipality derives revenue from rental or service. (State purposes separately.)	None
	None
4. Bonds issued, and authorized but not issued, for school purposes, after deducting sinking funds and funds in hand applicable thereto	4,983,827.10
5. Bonds issued, and authorized but not issued, for park purposes. (Note.—In the case of a county, deduct sinking funds and funds in hand applicable to such bonds)	None
6. Bonds issued, and authorized but not issued, not included above. (State purposes separately)	7,000,250.00
	None
	None
(*b*) *Evidences of indebtedness other than bonds.* (*Including temporary notes or bonds, issued under section thirteen of Chapter 252, P. L. 1916, as amended. Note.—Not including notes issued or to be issued in anticipation of taxes of the current fiscal year.*)	
1. Evidences of indebtedness issued, and authorized but not issued, for school purposes	2,874,400.00
2. Other evidences of indebtedness issued, and authorized but not issued	7,632,946.06
TOTAL GROSS INDEBTEDNESS	$40,571,682.83

B. DEDUCTIONS

The deductions are as follows:

(a) The amount of special assessments levied and uncollected, applicable to the payment of any part of the gross indebtedness not deducted under some other item hereof	$ 603,759.83
(b) The amount as estimated by resolution of the governing body of special assessments to be levied, which will be applicable to any part of the gross indebtedness not deducted under some other item hereof	Nothing
(c) Indebtedness incurred, and authorized but not incurred, for the purposes below stated (but not for the sup-	

port or maintenance thereof) separately stated in so far as separately issued for such purposes, the payment of the principal and interest of which indebtedness was adequately provided for from revenue from rentals or services rendered after deducting operating expenses during the previous fiscal year, namely:		
1. Docks	None	
2. Electric light or power	None	
3. Gas	None	
4. Markets	None	
3% of the average assessed valuation as stated in subdivision D hereof	$9,140,986.53	
Deductions under this item (c) (Insert smaller of above two amounts)		None
(d) Indebtedness incurred and authorized but not incurred, for the supply of water		14,650,254.72
(e) The net indebtedness incurred and authorized but not incurred, for school purposes as stated in A (a) 4, and A (b) 1	7,858,227.10	
3% of the average assessed valuation as stated in subdivision D hereof	9,140,986.53	
Deductions under this item (e) (Insert smaller of above two amounts)		7,858,227.10
(f) Funds in hand and sinking funds or such parts thereof as are held for the payment of any part of the gross indebtedness other than that which is included in these deductions or otherwise deducted. Under this item is included the proceeds on hand of any bonds or notes held to pay any part of the gross indebtedness and the estimated proceeds of bonds or notes which have been authorized if such estimated proceeds will be held for that purpose		5,165,320.64
(g) Amount included in the current taxes levied for the payment of any part of the gross indebtedness other than that which is included in these deductions		None
(h) Amount of unpaid taxes not more than three years in arrears		1,189,195.27
(i) Indebtedness incurred, and authorized but not incurred, for the construction or reconstruction of dikes, bulkheads, jetties, or other devices erected along the ocean or inlet fronts and intended to prevent the encroachment of the sea including the improvements to restore property damaged by the sea		None
(j) Amounts owing by the State, by other municipalities or by other persons or corporations on account of that part of an improvement (not an assessment improvement) for which indebtedness has been incurred or authorized and not deducted under some other item		None
TOTAL DEDUCTIONS		$29,466,757.56

C. THE NET DEBT

The net debt of the municipality as determined by deducting the deductions as stated in subdivision B from the gross debt stated in subdivision A is as follows:

Gross debt	$40,571,682.83
Deductions	29,466,757.56
NET DEBT	$11,104,925.27

D. AVERAGE ASSESSED VALUATION

The three next preceding assessed valuations of the taxable real property (including improvements) of the municipality and the average thereof is as follows:

1918 assessed valuation of such real property	$300,550,016
1919 " " " " "	301,689,039
1920 " " " " "	311,859,599
AVERAGE OF SUCH ASSESSED VALUATIONS	$304,699,551

E. PERCENTAGE OF NET DEBT TO AVERAGE ASSESSED VALUATION

The percentage that the net debt as computed under subdivision C hereof bears to the average of the assessed valuations computed under subdivision D hereof is as follows:

Three and 64/100 per cent (3 64/100%)

Supplemental Debt Statement of a New Jersey City

STATE OF NEW JERSEY } SS:
COUNTY OF HUDSON }

JAMES F. GANNON, Jr., being duly sworn deposes and says:

Deponent is the Director of the Department of Revenue and Finance of the City of Jersey City hereinafter called "the municipality" and the chief financial officer thereof. The supplemental Debt Statement annexed hereto and hereby made a part hereof is a true statement of the debt condition of the municipality on the date hereof and is computed as provided for the annual debt statement by Chapter 252 P. L. 1916, as amended.

Subscribed and sworn to before me this 25th day of July, 1921. } JAMES F. GANNON, JR.

ROBERT ORR
Commissioner of Deeds
for New Jersey.

A. (1) The net debt of the municipality as stated in subdivision C of the annual debt statement last filed is	$ 11,104,925.27	
(2) The amount by which such net debt has been { increased / decreased } is	737,111.96	
(3) The net debt at the time of this statement is		$ 11,842,037.23

B. The amounts and purposes separately itemized of the bonds or notes about to be authorized, together with the deductions which may be made on account of each such item:		
General Improvement Bonds	$ 2,275,000.00	
Proceeds thereof to be applied to existing indebtedness	2,266,000.00	
TOTAL under this Item B		9,000.00
C. The net debt of the municipality after the indebtedness to be authorized has been incurred is (NOTE—Add A and B)		11,851,037.23
D. The three next preceding assessed valuations of the taxable real property (including improvements) of the municipality and the average thereof is as follows:		
1918 assessed valuation	$300,550,016.00	
1919 " "	301,689,039.00	
1920 " "	311,797,199.00	
Average of assessed valuations		$304,678,751.00
E. The percentage that the net debt as computed under subdivision C hereof bears to the average assessed valuation computed under subdivision D hereof is as follows:		
Three and 89/100 per cent (3.89%).		

Summary Debt Statement of the Same New Jersey City

CITY OF JERSEY CITY, N. J.
FINANCIAL STATEMENT

Total outstanding bonds		$ 31,009,510
Water Bonds	$14,650,255	
Sinking funds and bond cash account other than for Water Bonds	6,002,185	20,652,440
NET BONDED DEBT		$ 10,357,070
Floating and temporary indebtedness (including Temporary Bonds issued, and authorized, but unissued)		10,487,345
TOTAL NET DEBT		$ 20,844,415
Less amount of floating or temporary indebtedness to be funded by bonds to be issued		864,000
		$ 19,980,415
BONDS TO BE ISSUED		864,000
NET DEBT, INCLUDING BONDS TO BE ISSUED		$ 20,844,415

ASSESSED VALUATIONS

Real Property, including Improvements	$319,075,528
Personal Property	50,772,250
TOTAL	$369,847,778

Chapter VII

THE PROMISSOR IN THE BOND

Bonds classified.—Most writers on municipal bonds separately classify bonds issued by the United States, the various States of the Union, counties and municipalities, the latter including quasi municipalities and taxing districts.

There is good reason for separate treatment of bonds issued by the Federal Government and the States, both of which have a peculiarity hereinafter referred to. There seems to be no adequate reason for treating bonds issued by counties differently from those issued by municipalities and quasi municipalities. Neither is there any adequate reason for treating together municipal and quasi municipal obligations. There is, indeed, better reason for a separate consideration of bonds issued by or supported by taxation of the latter class.

It will be remembered that legislatures, within certain limitations not here relevant, may endow counties and lesser political subdivisions with such powers as they will. The power to issue negotiable instruments being statutory, legislatures need not, and in fact do not, differentiate between counties and municipalities in this respect. There is technically no difference between the borrowing powers of cities and counties, except such as are created by the constitutions of the States. The same general principles governing fiscal legislation apply to counties and municipalities. The logical classification is first as to the promissor; second, as to the character of the promise.

Compulsory payment.—It has been well suggested that a proper classification is that based on means of payment, that is, whether payment is compulsory or not compulsory. This classification would distinguish, because of accepted principles, between bonds of a sovereign power (within which would be included the Federal and State Governments) and bonds of municipalities. There is, in strict legal contempla-

tion, no obligation upon the first class to pay its debts. The fulfillment of the promise of a government rests on good faith. When a municipality promises to pay, on the other hand, its promise may ordinarily be enforced. Certainly, it is within the power of a bondholder to sue the municipality and the courts will aid him to the full extent of their ability to enforce any judgment he may obtain.

Federal and State bonds.—Bonds of the Federal government and those of the various States are outside the scope of this book. Such bonds depend upon the good faith of the sovereign because the sovereign cannot be sued without its consent, although some States, such as New York, give their consent in advance. In New York State, any person may sue the State in the Court of Claims which is provided for the purpose, but there is no means of enforcing the judgment of the Court of Claims unless the legislature makes an appropriation.

Before dismissing the subject of State bonds as not strictly within our province, it may be said that although States do contract debt it may not be sound economic policy for them to do so except in aid of public enterprises requiring enormous sums of money. The building of the Erie Canal in New York State was in its day a colossal undertaking and the money was properly borrowed. The relatively recent enlargement of the Barge Canal was another such undertaking. Neither of these projects could have been paid for out of funds raised by taxation in one year, but appropriations for the building of State institutions, such as hospitals, should be, and in eastern States generally are, included in the annual budget appropriations.

County bonds.—Counties are at most but legal organizations which, for the purpose of safe administration, are vested with a few functions characteristic of a corporate existence. They are legal subdivisions of the State "created by the sovereign power of the State, of its own sovereign will, without the particular solicitation, consent or concurrent action of the people who inhabit them." * * * "With scarcely an exception, all the powers and functions of the county organization have a direct and exclusive reference to the general policy of the State and are, in fact, but a branch of the general administration of that policy." [1] County bonds are usually

[1] *Hamilton Co. v. Mighels* (1857), 7 Ohio St. 109.

issued for the construction of roads and bridges, court houses, jails and poorhouses.

There is no legal principal peculiarly applicable to the issue of county bonds. The questions for consideration are economic; that is, the real questions are those of taxing power and debt. In considering the latter we must remember that the same property which is taxed by the county for county purposes is taxed by municipalities for their own purposes and may be again taxed and yet again taxed by various minor subdivisions, but this is also frequently true of cities.

Contingent debt.—An item which is almost never considered is contingent debt, which may become real in case of default of a minor subdivision of the county. For example, in Virginia, bonds for road improvements may be issued by the county, payable from taxes levied in specified "magisterial" districts. The taxable property in such districts is primarily liable but the bonds are those of the county and the statutes provide that the county shall be liable in case of default. How its liability may be enforced is a different problem under the statutes authorizing such bonds. Under the decisions it is real liability, contingent, it is true, but liable to become actual.[2]

True municipalities.—As our inquiry is largely directed toward ascertaining the powers of true municipalities to issue negotiable instruments, we may dismiss the obligations of such at this point with the understanding that according to the weight of authority a municipal corporation having ordinarily full powers may have implied power to borrow for municipal purposes but it must have express statutory power to issue negotiable securities.

Quasi municipalities.—"Civil corporations are of different grades or classes. * * * The school district or road district is usually invested by general enactments operating throughout the State with a corporate character, the better to perform within and for the locality its special function, which is indicated by its name. It is but an instrumentality of the State and the State incorporates it that it may the more effectually discharge its appointed duty. * * * Considered with respect to the limited number of their corporate powers, the bodies above named," that is, quasi municipal corporations, "rank low down in the scale or grade of corporate existence;

[2] *Moss v. Tazewell County* (Va. 1911), 112, Va. 878; 72 S. E. 945.

and hence have frequently been called *quasi* corporations. This designation distinguishes them on the one hand from private corporations aggregate, and on the other from municipal corporations proper, such as cities or towns acting under charters, or incorporating statutes, and which are invested with more powers and endowed with special functions relating to the particular or local interests of the municipality, and to this end are granted a larger measure of corporate life." [3]

Quasi corporations classified.—A classification of quasi municipal corporations, which is suggested by the actual facts, is as follows:

(a) Those which may borrow and tax.
(b) Those which may borrow but not tax.
(c) Those which may be taxed but may not borrow.

Those which may borrow and tax.—In the first class, that is those which may both borrow and tax, we can place school districts, the boards of education ordinarily being bodies corporate, which when a tax has been levied, as in New York, to be collected in installments, may issue bonds payable in the same years as the installments of tax are to be levied. Under this classification also fall irrigation, levee, and drainage districts. The Miami Conservancy District in Ohio, for example, has been incorporated for the purpose of enabling the people within the drainage area of the Miami River to issue bonds and protect themselves against floods and washouts. Another well-known example of a specially organized political subdivision is the Chicago Sanitary District. The district was incorporated to enable a section of the State to construct and finance drainage canals and other works for the protection of the public health. In connection with such securities it is well to bear in mind that the borrowing power must be accompanied by the taxing power. Otherwise the district would lack the means of obtaining revenues to meet the charges on its debt. No incorporated political district can assign its rights to tax or borrow to another organization, since it is a firm legal principle that a delegated power cannot be re-delegated.[4]

Those which may borrow but not tax.—There are probably very few quasi corporations which may borrow but may

[3] Dillon, p. 67.
[4] Sakolski, p. 87.

not tax. The Passaic Valley Sewer Commission in New Jersey is a quasi corporation of this character; its funds are derived from payments made to it by the various municipalities in the sewer district with which it has contracts, but in anticipation of the receipt of funds it may incur temporary debt.[5] The general scheme of financing the Passaic Valley improvement will well repay consideration by the student. Its peculiar characteristic (that it may not tax) is caused by a constitutional provision in New Jersey to the effect that a taxing district must be co-terminus with a political subdivision and that a political subdivision cannot be divided or subdivided to form a tax district.[6]

Those which may be taxed but may not borrow.—Quasi municipal corporations which may be taxed but may not borrow are of the type of which Virginia "magisterial" districts are examples. Bonds for road improvements in such districts are issued by the county. The funds to pay the bonds are derived from taxes levied upon property in the district. Hence we can say that such quasi corporations may be taxed but may not borrow.[7]

From the investor's viewpoint the distinction between bonds of counties, cities, quasi municipalities and taxing districts is most important. The particular features of the bonds of different promissors will be considered in subsequent chapters.

[5] P. L. 1907, p. 31, Sec. 7.

[6] *Van Cleve v. Sewer Commissioners* (N. J. 1903), 71 N. J. L. 574; 60 Atl. 214.

[7] See Laws of Virginia, 1908, Chap. 70.

Chapter VIII

THE PROMISE AND THE PURPOSE OF THE BOND

The greatest concern should be shown by the underwriter or investor as to the character of the promise made by the bond. No matter how limited or special the means of payment, the municipal bond is on its face an unlimited and unqualified promise to pay. This is so except in the rare case of an honestly drawn assessment bond which may state on its face that the amount promised is payable only from a certain fund or taxes levied in a certain area, less than the territory included in the issuing unit.

Debt limit.—The debt limit does not affect the character of the promise because the debt limit is or is not exceeded at the moment of issue.

If an issue of bonds is within the debt limitation when issued, it remains so and if its life is extended by refunding, it does not lose this characteristic.[1] A municipality may issue bonds within its limit, become indebted in excess of it, and lawfully refund the bonds issued before the limit was reached, without increasing its debt, and the bonds issued to refund the old debt will be valid. This assumes proper statutory authority to refund.

Whether a subsequent reduction of the debt operates to validate bonds issued in excess of the limitation of indebtedness may depend upon constitutional or statutory provisions, the effect of the estoppel, if any, contained in the form of the bond, and upon the circumstances of the case. If the constitution or statute provides that indebtedness issued in excess of the limitation shall be absolutely void, then a reduction of the debt so that the bonds in question fall within the permitted limitation, would not make the bonds valid. It is possible that they might be enforced but a discussion of the circumstances under which this would be possible will carry us too far into problems of law. The point to be observed

[1] *Poughkeepsie v. Quintard* (1892), 136 N. Y. 275.

is that questions of limitation of indebtedness do not affect the character of the promise made by the bond.

Limited taxation.—A limited tax rate results in a limited obligation. Where the power to tax to pay a bond is limited, the obligation, that is, the bond, is a limited obligation. This is well illustrated by the decision of the Supreme Court of the United States in *United States v. County of Macon.*[2] The statute authorized railroad-aid bonds and provided for the levy of a tax to pay the same not exceeding one-twentieth of one per cent upon the assessed value of the taxable property of each year. Default having occurred, the bondholder recovered judgment upon interest coupons, execution was issued, and the judgment returned unsatisfied. The owner of the coupons asked for a writ of mandamus directing the county court to levy and collect a tax for the purpose of paying the judgment. Mr. Chief Justice Waite said:

"Every purchaser of a municipal bond is chargeable with notice of the statute under which the bond was issued. If the statute gives no power to make the bond, the municipality is not bound. So, too, if the municipality has no power, either by express grant or by implication, to raise money by taxation to pay the bond, the holder cannot require the municipal authorities to levy a tax for that purpose. If the purchaser in this case had examined the statutes under which the county was acting, he would have seen what might prove to be difficulties in the way of payment. As it is, he holds the obligation of a debtor who is unable to provide the means of payment. We have no power by mandamus to compel a municipal corporation to levy a tax which the law does not authorize. We cannot create new rights or confer new powers. All we can do is to bring existing powers into operation. In this case it appears that the special tax of one-twentieth of one per cent has been regularly levied, collected, and applied, and no complaint is made as to the levy of the one-half of one per cent for general purposes. What is wanted is the levy beyond these amounts, and that, we think, under existing laws we have no power to order. . . . We have not been referred to any statute which gives a judgment creditor any right to a levy of taxes which he did not have before the judgment. The judgment has the effect of a judicial determination of the validity of his demand and of

[2] (1878), 99 U. S. 582.

the amount that is due, but it gives him no new rights in respect to the means of payment."

The reasoning of this opinion has been followed by the courts of last resort of several States.

Constitutional limitations.—It should be noted that if the tax limitation is contained in the State constitution, the bondholder may be in a very unpleasant predicament because there is no ready means of relief. It is a difficult matter to amend State constitutions and they are not ordinarily amended to relieve a creditor. If the limitation is by statute, an appeal may be made to the legislature, which in a proper case and in the absence of any constitutional prohibition may very properly give the bondholder relief by repealing the limitation or raising the limit. On this subject Mr. Chester B. Masslich, a well-known specialist, has said:

"Perhaps the worst form of tax limitation is the general limitation which fixes the maximum rate of annual tax for all purposes. If the amount raised by such a tax is insufficient to pay running municipal expenses and also the principal and interest of outstanding bonds, the courts hold that the payment of running expense comes first, and that the creditors can have no part of the taxes which the municipal authorities in their discretion choose to apply to those expenses. In other words, the maintenance of the life of a municipality is its first duty and the courts will not disturb the judgment of its governing body as to the amount necessary for maintenance.

"There are many laws on the statute books today which fix so high a limit upon the amount of bonds which may be issued, and so low a limit upon the amount of taxes that may be levied to pay them, that it is a foregone conclusion that the bonds will not be enforceable if the entire amount allowed by law be issued. . . .

"North Carolina is one of the States which have seen the error of limits upon bond taxes. With few exceptions, all the general and special laws passed in that State in recent years granting authority for bond issues, have expressly provided that the tax for their payment shall be unlimited. South Carolina has followed the same new policy. Georgia has long since removed all limits upon bond taxes by constitutional enactments which make mandatory a sufficient levy without any limit whatever, and as a result the bonds of

Georgia counties and municipalities find a ready sale. Georgia's taxpayers have not suffered, for the same section of the constitution which requires the unlimited tax puts a rigid limit upon the amount of lawful debt that may be created.

"Across the line from Georgia, Alabama still labours under a constitutional limit of bond taxes, with the result that investors pay little attention to public securities coming from that State." [3]

Legality independent of power to pay.—It is a curious fact that the validity and legality of a bond may be independent of the power to pay it. In one jurisdiction this doctrine was at one time applied. The Supreme Court of North Carolina said in substance that a bond may be in all respects validly and legally issued and constitute a valid obligation of a municiplity even though a sufficient tax levy to provide for the payment of principal and interest has not been, and possibly cannot be, made.[4] This ought not to be so, and it is reassuring to observe that the doctrine has been repudiated in the same jurisdiction.[5]

Assessment bonds.—These may be limited to specified funds. Usually they are issued to provide the funds for local improvements, such as sewers or sidewalks. The property benefited becomes liable for all or part of the cost of the improvement. The municipality undertakes only to levy the assessments which are to provide the fund for repayment. If the value of the property benefited and liable should not be sufficient to meet the obligation, the municipality would not have any further liability.

This is true only where the faith and credit of the municipality are not pledged to the payment of the debt, or where the municipality has not the power by statute to pledge its faith and credit. Assessment bonds issued in New York and New Jersey are, as between the bondholder and the municipality, general obligations of the municipality, supported by its unlimited taxing power. As between the municipality and the property owner, however, the property especially benefited must pay the bonds.

[3] Quoted in the *Daily Bond Buyer,* December 5, 1921.
[4] *Pitt County v. MacDonald* (N. C. 1908), 148 N. C. 125; 61 S. E. 643.
[5] *Proctor v. Nash County* (N. C. 1921), 108 S. E. 360.

Assessment bonds not negotiable instruments.—Where the instrument is payable solely from a special fund, the bonds are not negotiable instruments.

"Respecting the question of the negotiability of these instruments, it has been held that because the bonds are not payable unconditionally and at all events, but only out of a special fund created for and pledged to the payment, which may or may not prove adequate to meet the obligations in full, they do not have that certainty of payment which is essential to negotiability, and that they are not negotiable instruments within the Law Merchant. Being deprived, according to these decisions, of one of the characteristics of negotiability by the uncertainty of payment, improvement bonds of this nature have been held to be mere *choses in action,* and in the hands of a purchaser for value, without notice, subject to all the defenses to which they are subjected in the hands of the contractor or person to whom they were originally issued." [6]

As pointed out in Chapter I, consequences important to the bondholder follow the negotiability of the instrument. Unless the bond is fully negotiable, it is not in fact a municipal bond as the term is employed, and it should not sell on the same basis as a fully negotiable bond.

Federal tort theory.—An interesting gloss on this statement is afforded by consideration of a doctrine which Frederick P. Delafield has aptly named the "Federal Tort Theory." Briefly stated, it is this: If a municipality makes a contract or issues a bond payable only from assessments and then fails to levy the assessments or to collect them, the municipality becomes liable.[7] The consequences of this theory are extremely interesting, but belong to a more exhaustive consideration of the subject than can be given here.

In Chapter XI it is pointed out that the bondholder may obtain the money represented by the bond in an action on contract where the bond is not enforcible as such.

Limitation of area.—Limitation because of the area taxed, is illustrated by issues of New York town bonds for sewer purposes. Under the law [8] sewer districts may be organized and the property within them assessed to pay the cost of the

[6] Dillon, p. 1392.
[7] *Barbour Asphalt Co. v. Denver* (1896), 72 Fed. 336.
[8] Cons. Laws, Chap. 62, Sec. 360.

improvement. The bonds, however, are issued by the town which is only secondarily liable and may be held liable only if there is a shortage in the primary fund.

In conclusion we may say that a true municipal bond must contain a full and unqualified promise to pay, not only in words but in contemplation of law. The opinion of counsel is understood to mean that there is such a promise. An Ohio court has recently said:

"But I assume that 'legality' means something more than the mere formality of issue. *It means the expression of a perfect obligation;* that the bonds shall not be merely the expression according to legal form, perfect in its intonation and following all the regulations; but that the result of these formalities shall be the creation of an obligation on the issuing of those securities that is perfect so that the buyer shall have no concern about the security returning both his income and investment. That, therefore, involves the construction of the entire law that relates to the creation of the obligation and in the opinion of counsel the limitations which the laws of Florida fix upon a municipality are such that in this case there is an imperfect obligation. That is precisely the question intended to be submitted to him; so that he has expressed the sentiment of those who deal in these securities and given to the purchaser the opinion of the profession with regard to the security that the obligation created. Now it matters not that these bonds could be pursued to a judgment. You may have as many judgments as you can get, but only one satisfaction. It is not the ability to secure a judgment, but it is the perfection of the security of the investment which constitutes its legality; and here counsel, in good faith and true to their client, have given their opinion that they should not approve the bonds." [9]

As a mere matter of mathematics, a limited tax rate may produce ample revenue to run the municipality and to provide funds for debt service, but increasing demands for general service or a conflagration or a flood may impair the margin of safety or even destroy the value of taxable property. The municipal revenue may diminish and as the municipality must live before it pays its debts, a default must inevitably result.

Purpose of issue.—Text writers have classified bonds as

[9] *A. T. Bell v. Plant City, Fla.* Decision not reported; Lucas Co., Ohio, Common Pleas, Oct. 7, 1920.

to purpose. This classification has no meaning, except that bonds issued for self-sustaining or partially self-sustaining public utilities have a factor of safety that bonds issued for non-revenue producing improvements may not have. Water works, especially systems operated by gravity, should produce enough revenue to pay operating expenses and the interest and principal of maturing bonds. This is recognized by many statutes, which permit deduction of such bonds in computing the borrowing power of the municipality. The same principle extends to bonds issued for wharves, docks and markets. A familiar example exists in bonds issued by New York City for the purpose of securing funds for the construction of rapid transit facilities. Under properly drawn statutes, such bonds may be deducted in computing borrowing power only to the extent that the income from the utilities provides sufficient funds for debt service. When such income becomes insufficient, the bonds must be charged against the limit of indebtedness. In a limited sense, streets and sewers, schools, hospitals and parks add to the revenue-producing power of the municipality, but so very remotely as not to affect the means of payment or security for the bonds.

Term of bonds.—Term in relation to purpose is considered in Chapter IX devoted to term and serial bonds.

Chapter IX

THE MATURITY OF THE BOND

Classification according to time of payment.—Classification of bonds may be according to the time of payment, or maturity, one of the most important factors in determining price, which is considered in Chapter XIV.

Short-term loans.—Bonds, certificates of indebtedness, or notes, running, let us say, less than five years, are called short-term obligations, and are considered from a far different angle than are the long-term or serial bonds. The short-term loan is usually self-liquidating, being issued in anticipation of taxes or other revenues, and commercially is treated as a liquid asset. Our concern is not with short-term loans as such.

Determination of time of payment.—The time of payment of any bond depends upon the language of the statute authorizing it, for the reason that most statutes prescribe a maximum maturity for bonds, and a bond which purports to run for longer than the permitted term is illegal. While certain classes of foreign government securities are not payable at any definite time, it has been the practice, as well as the law, ever since American municipalities have been issuing bonds, to make them absolutely due and payable within a relatively limited period of years. Very few municipal bonds have a life of over fifty years from the date of issue. Considered as to maturity, bonds are of two kinds:

Term bonds.—Term bonds are those of an issue of which all the bonds become due and payable at one time. For example, $100,000 bonds dated May, 1922, may all mature and be due and payable May 1, 1952, in which case the term or life of the bond is 30 years. For the reasons hereafter referred to, the issue of term bonds is becoming less and less frequent and the issue of serial bonds is made mandatory by statute.

Callable bonds.—Callable bonds, sometimes called redeemable or optional bonds, are term bonds which may be

called for payment before their maturity. This is in order that the issuing municipality may redeem its indebtedness if it chooses to exercise the option, without being obliged to do so. Such bonds may be redeemed, if the issuing municipality so decides, 15 or any number of years after their issue, but may not be absolutely due and payable until, for example, 30 years thereafter. A bond redeemable after 15 years and payable at the end of 30 years after issue is called a "15-30." So a bond redeemable in 5 years and payable in 20 years after issue would be called a "5-20."

Notice of prior redemption.—The bond form should contain a provision that the issuing municipality, if it desires to exercise its option of prior redemption, will give notice to the bondholder a certain number of weeks or months in advance of the optional date. Provision is usually made to give this notice by publication in one or more designated financial newspapers. As a matter of fact, such notice, called constructive, is not always brought to the attention of the bondholder. Notice of intention to redeem is intended to enable the municipality to call the bonds for payment, and interest usually stops with the giving of such notice. The notice also permits the bondholder, if he is fortunate enough to receive it, to find a new investment for his money, as he has been warned that his bonds will be paid.

The issue of callable bonds indicates a very high degree of optimism upon the part of the municipal officials. Very few of such bonds are called for payment before their maturity. They do not sell at the same price as they would for the term without the optional feature, since for the purpose of computing the selling price or basis, the bond is treated as running only to the optional date and not to maturity. Thus a "15-30" bond sells as though it were a 15-year term bond. Such bonds are not as desirable as the straight term or serial bond.

Sinking funds.—It has been explained that bonds are paid from the proceeds of taxation. If a municipality was permitted to issue a considerable amount of bonds to run for several years, with no provision for the payment of the bonds before they mature, the amount of money which would have to be raised to pay the bonds in the year of their maturity would not only send the municipal tax rate sky-rocketing, but the amount might conceivably be so large that it could not be

raised by taxation. Hence, at an early period, the principle of the sinking fund was applied to municipal financing. A sinking fund is formed by setting aside a sum of money at stated intervals to provide for the payment of all or part of the principal of a debt. It is a method of sinking or extinguishing it; a provision for an obligation not yet matured. The practice may be illustrated by saying that, if a bond runs for 30 years, 3 1/3% of the amount of the bond is annually included in the tax levy, and when the tax is paid, the amount is turned over to a particular municipal official, or a group of officials, called the Sinking Fund Commission. Statutes which permit the issue of term bonds require such provision for the payment of the bonds to be made. If the ordinance or statute authorizing the bond issue provides for a sinking fund, this provision is part of the contract between the municipality and the bondholder, and the rights of the latter to insist upon the protection of the sinking fund cannot be impaired by any subsequent legislative enactment [1] or act of the issuing municipality. This is so because of the constitutional guarantees against impairing the obligations of contracts. A standard sinking fund clause or contract follows this chapter, and an examination of it will show the principles upon which the sinking fund operates.

Annual contributions to sinking fund.—The amount raised each year for sinking fund purposes is determined arithmetically, and various tables are used to compute the amount. The table authorized by the commissioner of municipal accounts in New Jersey computing on a 3½% annual cumulative basis is given at the end of this chapter following the model sinking fund clause above referred to. The annual sinking fund requirements for the issue of term bonds is found by multiplying the amount opposite the stated term of the issue, by the number of one-thousand-dollar bonds; thus, referring to the table, it will be seen that if a one-thousand-dollar bond runs for five years, the amount contributed annually will be $186.4814. The table assumes that interest on the sinking fund investments will be compounded semi-annually. The annual contributions to the sinking fund must be invested promptly, together with the interest on all sinking fund investments, at a rate of return at least equal to the percentage used in the table fixing the annual contribution,

[1] Dillon, p. 195.

in order to produce the necessary amount at the date of maturity.

Misuse of sinking funds.—Simple as all this is in theory, the difficulty with the sinking fund plan is that it is not carefully followed and observed except in the best municipal families. "To the student of municipal finance, with a sense of humour," says Professor Jordan, "city sinking funds afford a subject of pleasurable research. Sinking funds have been notoriously misused for purposes absolutely foreign to their object. * * * Many cities require that sinking fund moneys be used exclusively for the purchase of bonds of the same city, without requiring that the bonds be of the same issue as that for which the fund is created. The city, desiring money at a later date, figuratively takes some new bonds out of its right-hand pocket and exchanges them for sinking fund cash in its left-hand pocket, and thereupon proceeds to pay itself interest on the bonds. Such a transaction scarcely belongs to the twentieth century." [2]

For a city to invest its sinking funds in its own securities, suggests an individual securing his promissory note by the deposit of another. By doing so, it withdraws cash raised for the protection of the bondholder. It is hardly necessary to call to mind the plan of the comptroller of the State of New York to pay the soldiers' bonus from moneys on hand in the sinking fund, and later to reimburse the sinking fund when the bonus bonds were sold.[3] This happy thought was upset by a hard-hearted court of appeals which declared the State Bonus Bond Act unconstitutional.

Advantages of the sinking fund.—But a sinking fund which is not properly managed, or of which the principal is not kept at par, is better than none at all. The psychological effect on the minds of officials should not be ignored, for a consideration of sinking fund requirements when the annual budget is being made up is a reminder that debts must be paid. Sinking fund trustees are held to a very high degree of accountability and the investment banker who merchandises an issue of sinking fund bonds may well consider that he has at least a moral duty to remind officials that the annual contribution must be raised and paid in.

One great advantage which the sinking fund plan has is

[2] Jordan on Investments, p. 81.
[3] *The Daily Bond Buyer,* Sept. 3, 1921.

that the annual payments for interest and principal remain constant each year from the date of issue to the date of payment.

Under the sinking fund plan a uniform tax rate over a period of years will pay the interest and retire the bonds when they become due, provided the assessed valuation remains constant. As taxable valuations usually increase rapidly after extensive improvements have been made, there does not appear to be any particular advantage in a uniform tax rate. The tax rate will adjust itself to the valuation of taxable property and the needs of the community.

Serial bonds.—Serial bonds are those which mature in substantially equal annual installments during the life of the issue. A certain number therefore are redeemed annually, through application of the proceeds of taxes raised for that purpose. The serial plan of payment is an advantage because it avoids the sinking fund which is frequently open to so much criticism.

Equal annual installments.—Serial bonds are frequently required to be made payable in equal annual installments. This is to be avoided if possible, for such a rigid requirement frequently compels the municipality to issue bonds of odd denominations and sometimes in principal amounts expressed partly in cents. For example, a small issue payable in equal annual installments may mature $1,142.34 in each year. If the statute uses the expression "substantially equal annual installments," there is no necessity for such meticulous accuracy. It may be observed that where all the bonds of a municipality are required to mature in the same number of equal annual installments, as is the case with New York and Pennsylvania second class cities, a fairly even debt service results. The increased borrowing each year is offset by payments of principal and increases in assessable valuations.

The custom of issuing serial bonds is becoming increasingly common. It is mandatory in Massachusetts, New Jersey, New York, North Carolina, and many other States. The price is based on the average of the price of each maturity, figured separately. An issue maturing one thousand dollars a year for twenty years will have an average maturity of substantially ten years.

For an illustration of the prices of different maturities of the same issue of bonds, see copy of the advertisement appear-

ing on page 144. When securities sell above par, the longer the maturity the higher the value of the bond, since the time is longer in which to amortize the premium.

Advantages of the serial bond.—The great advantage of the installment bond is that no sinking fund with its attendant abuses is necessary or possible. In a sense, the serial plan is an automatic, mathematically correct sinking fund. That is, the amount required to be raised by taxation each year for debt service is the principal of the bonds maturing that year plus the interest payable during that year on all the bonds of the issue then outstanding and unpaid. The last table following this chapter shows the difference between the average annual cost and the total cost of sinking fund and serial bonds. In the table the sinking fund is assumed to be invested and compounded annually at 3½% where the coupon rate on the bonds to be paid is 5%. In practice it is doubtful whether any but the most expertly managed sinking funds are invested to yield more than an average of 3½%. Mathematically, the burden of taxation for the payment of serial bonds is identical with the cost under the sinking fund plan, if the sinking fund earns and is compounded at the same interest rate as is borne by the bonds.

Before dismissing the subject of sinking funds, attention is called to the copy of the annual report of the Sinking Fund Commission of Clifton, New Jersey, dated December 31, 1921, which follows this chapter. This is displayed not necessarily as being a model, but as showing clearly the operation of a sinking fund in a small city, subject to extremely strict statutory regulations of sinking funds.

Deferred serial plan.—Under the serial plan, a certain amount of the bonds is retired each year, the interest is paid on the remaining amount outstanding, and the retired bonds cease to be an interest charge on the community. The straight serial method requires the heaviest payments for interest and retirement of principal in the early years of the bond issue, often before the improvement is fully completed or before it has yielded the community any advantage. To meet these conditions, which frequently arise, the use of the deferred serial bond has become common. With such a modified type, no principal is retired until a certain period, usually five years, has elapsed. During this period, interest is paid but nothing more. Thereafter, the principal is re-

tired by uniform amounts and the interest charges are met, just as in the case of serial bonds having a term shorter by five years, or whatever the deferred period may be. In this way the municipality pays nothing but interest until the improvement is completed and taxes are levied and collected. Interest may be paid from principal during the construction period. The postponement of the payment of principal is particularly important when the bonds are paid from assessments, as is the case with irrigation district or similar issues.

Term related to life of improvement.—The statutes of some jurisdictions, like New Jersey, North Carolina, and Massachusetts, provide that the maximum life of the bonds shall not exceed the life of the improvement, such life being arbitrarily determined by statute or by the certificate of an official, such as the city engineer. The New Jersey [4] and North Carolina [5] bond acts contain elaborate provisions, giving the maximum terms of bonds which may be issued for different classes of public improvements. Under the New Jersey act, for example, bonds issued for the construction of a fire-proof building (which is carefully defined) must mature within forty years and those for the construction of a road of sand or gravel must mature within five years.

The New Jersey and North Carolina statutes provide that where bonds are to be issued for more than one improvement, an average shall be computed, taking into consideration the probable life of each improvement and the amount of money required therefor.

It is believed that the best modern thought on the subject of municipal financing requires that the term of bond issues shall not exceed the life of the improvement, so that the burden of the improvement will not have to be borne by persons who do not enjoy its benefits. It is also obvious that the longer the bonds run, the greater the interest charge, which in the case of bonds having a long term, may greatly exceed the principal itself.

Sinking Fund Clause or Contract

Until the principal and interest of the bonds shall be fully paid, there shall be raised and collected annually by tax upon all of the taxable property in the municipality, beginning with the next tax levy a sum sufficient to pay the inter-

[4] P. L., 1817, p. 803.
[5] Appendix B.

est on all of said bonds outstanding, as such interest becomes due and a further sum to be paid into a sinking fund sufficient to retire said bonds at maturity. The amount to be raised annually to pay the interest on said bonds shall be not less than the amount of one year's interest on the amount of bonds outstanding. The amount to be raised in the next annual tax levy for said sinking fund shall be at least.....dollars for each one thousand dollars of said bonds, and thereafter the trustees of the sinking fund shall each year ascertain the amount of said fund by appraising the securities held for investment therein at their fair market value not exceeding par, and shall determine the amount of money which, if thereafter annually contributed to said fund, would with the fund and with the accumulations thereon and upon the contributions thereto, such accumulations being computed at the rate of four per centum per annum, produce at the date of maturity the amount of the bonds outstanding, and the amount of money to be raised and contributed to said sinking fund in such year shall be at least the amount thus determined. If the income of the sinking fund in any year be more than the sum which, if annually added to the said fund, would, with the fund and its cumulations as aforesaid, retire the outstanding bonds at maturity, the excess income may then be applied to the interest on the bonds. If the sinking fund shall equal in amount the bonds outstanding, no further contributions need be made thereto except to make good any loss ascertained at the annual appraisals and the income thereof shall be applied to the payment of the interest on said bonds. The sinking fund shall be separately kept and shall be safely invested under the direction of the trustees thereof in securities in which savings banks of this municipality are by law authorized to invest or shall be applied to the purchase or cancellation of the bonds aforesaid. No moneys raised for the payment of the principal and interest of said bonds shall be appropriated or used for any other purpose.

Table Showing Annual Sinking Fund Requirements for Each $1,000 Bond

Term (years)	*Amount*
1	$1,000.0000
2	491.4005
3	321.9342
4	237.2511
5	186.4814
6	152.6682
7	125.5445
8	110.4767
9	96.4460
10	85.2414
11	76.0920
12	68.4840
13	62.0616
14	56.5707
15	51.8251
16	47.6848
17	44.0431
18	40.8168
19	37.9403
20	35.3611

Term (years)	*Amount*
21	33.0366
22	30.9321
23	29.0188
24	27.2728
25	25.6740

Table Showing Comparative Cost of Serial and Sinking Fund Plans[6]

$100,000 5% BONDS

	ANNUAL AVERAGE DEBT SERVICE		TOTAL COST	
Maturing in years	*3½% Sinking Fund*	*Serial*	*3½% Sinking Fund*	*Serial*
5	$23,648	$23,000	$118,241	$115,000
10	13,524	12,750	135,241	127,500
15	10,183	9,333	152,738	140,000
20	8,536	7,625	170,722	152,500
25	7,567	6,600	189,185	165,000
30	6,937	5,917	208,114	177,500
35	6,500	5,429	227,494	190,000
40	6,183	5,063	247,309	202,500
45	5,945	4,778	267,540	215,000
50	5,763	4,550	288,169	227,500

Sinking Fund Commission
Clifton, New Jersey

December 31, 1921.

To the City Council of the City of Clifton,
New Jersey.

Gentlemen,—In accordance with the requirements of the Sinking Fund Law of the State of New Jersey, the Sinking Fund Commission of the City of Clifton herewith transmits its statement of the Sinking Fund account for the year 1921.

BALANCE ON HAND JANUARY 1, 1921

Cash on Deposit, Clifton Trust Co	$ 111.63
$32,000 U. S. L. Bonds Second Issue 4¼	28,934.97
$ 2,000 U. S. L. Bonds Third Issue 4¼	1,871.60
$15,500 U. S. L. Bonds Fourth Issue 4¼	14,733.24
Total Sinking Fund, January 1, 1921	$45,651.44

RECEIPTS FOR YEAR 1921

Mar. 21.	Interest on $ 2,000 Third Liberty Bonds	$ 42.50
Apr. 18.	Interest on $14,000 Fourth Liberty Bonds	297.50
Apr. 18.	Interest on $ 1,500 Fourth Liberty Bonds	31.87
May 18.	Interest on $32,000 Second Liberty Bonds	680.01
Sept. 23.	Interest on $ 2,000 Third Liberty Bonds	42.50
Oct. 19.	Interest on $15,500 Fourth Liberty Bonds	329.38
Nov. 21.	Interest on $33,000 Second Liberty Bonds	701.24
Nov. 1.	Interest on Bank balance to Nov. 1, 1921	6.87

[6] From *Engineering News-Record*, August 30, 1917.

1921 Appropriations for Sinking Fund

Dec.	8. From City Treasurer—General Bonds	3,118.78	
Dec.	8. From City Treasurer—School Bonds	4,679.46	
Dec.	8. From City Treasurer—Special Sinking Fund	3,772.78	
Total Receipts Year 1921.....			$13,702.89
DISBURSEMENTS:			
July 7.	Accrued Interest on purchase $1,000 Second Liberty Bonds	6.26	
Dec. 8.	Accrued Interest on purchase $13,000 Second Liberty Bonds	36.83	
Total Disbursements		$ 43.09	
Net Amount Added to Sinking Fund.....			13,659.80
NET SINKING FUND DECEMBER 31, 1921.....			$59,311.24

INVESTMENTS HELD BY COMMISSION

On December 31, 1921, the total Sinking Fund of $59,311.24 was invested as follows:

$46,000 Par Value U. S. Second Liberty Bonds, 4¼.....	$42,436.22
$ 2,000 Par Value U. S. Third Liberty Bonds, 4¼.....	1,871.60
$15,500 Par Value U. S. Fourth Liberty Bonds, 4¼.....	14,733.24
Balance in Clifton Trust Co., December 31, 1921.....	270.18
	$59,311.24

Average Rate of Interest on Investments 4.57549 per cent.

The following statement shows the amount of sinking fund monies credited to the various issues of long term bonds as of December 31, 1921, in comparison with the amounts that should have been available on that date for each issue under the law:

	Legal Requirements	Amount in Sinking Fund	Surplus Over Legal Requirements	Deficit Below Legal Requirements
GENERAL BONDS				
$131,000 Trunk Sewer, 4½.....	$19,741.34	$20,167.50	$ 426.16	.....
$ 30,000 Municipal Bldg., 4½....	4,520.92	4,678.79	157.87	.....
$ 50,000 Tem. Sew. Bds., 6%, dated July 1, 1921	.....	.....	.....	.....
SCHOOL DIST. BONDS				
$95,000 School, 4½, dated May 1, 1914	31,644.69	14,914.25	.....	16,730.44
$19,900 Three Issues, School, 4½, May 1, 1907.....	11,405.31	2,517.87	.....	8,887.44
$28,000 Two Issues, School, 5%, July 1, 1908.....	10,471.51	1,855.97	.....	8,615.54
SPECIAL SINKING FUND				
To wipe out deficit— School Bonds		15,176.86	15,176.86	.....
	$77,783,77	$59,311.24	$15,760.89	$34,233.42

SUMMARY

Legal Requirements		$77,783.77
Amount in Sinking Fund	$ 59,311.24	
Deficit to be taken care of through Special Sinking Fund	18,472.53	
		$77,783.77
Deficit	$34,233.42	
Surplus	15,760.89	
	$18,472.53	

Annexed to this report is detailed information concerning the funded indebtedness of the City of Clifton.

The Sinking Fund Commission has authorized the Secretary of the Commission to have this report printed in full for distribution in accordance with the Sinking Fund law.

Respectfully submitted,

SINKING FUND COMMISSION:

.....

(Member ex-officio)

.....

(Term expires.....)

NO APPOINTMENT

.....

TOTAL BONDED DEBT OF THE CITY OF CLIFTON, N. J.

The entire bonded debt of the City on December 31, 1921, was as follows:

General Bonds:		
Temporary Sewer Bonds 6%, 1927	$ 50,000	
Trunk Sewer 4½'s, 1945	131,000	
Trunk Sewer 5's Serial	25,000	
Municipal Building 4½'s, 1945	30,000	
Total General Bonds		$236,000
School Bonds:		
Sinking Fund Bonds	$142,900	
Serial Bonds	425,000	
Total School Bonds		$567,900
Total bonded debt December 31, 1921		$803,900

The bonded debt of the City of Clifton was increased during the year 1921 by $155,000 net.

STATEMENT SHOWING THE AMOUNT OF BONDS TO BE PAID OFF ANNUALLY AND THE AMOUNT OF INDEBTEDNESS AT THE END OF EACH YEAR, BASED ON THE INDEBTEDNESS AS OF DECEMBER 31, 1921

Year	*Serial Bonds to be paid off*	*Bonds to be paid off through Sinking Fund*	*Bonded Indebtedness December 31 each year after payments*
1922	20,000	.....	783,900
1923	19,500	1,000	763,400
1924	19,500	1,000	742,900
1925	18,000	1,500	723,400
1926	18,000	6,000	699,400
1927	18,000	56,000	625,400
1928	18,000	6,000	601,400
1929	18,500	6,000	576,900
1930	18,500	7,000	551,400
1931	14,000	9,000	528,400
1932	14,000	9,000	505,400
1933	14,000	9,000	482,400
1934	14,000	9,000	459,400
1935	14,000	9,000	436,400
1936	14,000	8,400	414,000
1937	14,000	7,000	393,000
1938	14,000	7,000	372,000
1939	14,000	7,000	351,000
1940	14,000	7,000	330,000
1941	12,000	7,000	321,000
1942	13,000	7,000	291,000
1943	13,000	7,000	271,000
1944	13,000	6,000	252,000
1945	12,500	161,000	78,500
1946	12,000	.....	66,500
1947	11,000	.....	55,500
1948	8,000	.....	47,500
1949	6,000	.....	41,500
1950	5,000	.....	36,500
1951	5,000	.....	31,500
1952	4,500	.....	27,000
1953	3,000	.....	24,000
1954	3,000	.....	21,000
1955	3,000	.....	18,000
1956	3,000	.....	15,000
1957	3,000	.....	12,000
1958	4,000	.....	8,000
1959	4,000	.....	4,000
1960	4,000	.....	.....
	$450,000	$353,900	

Serial Bonds	$450,000
Sinking Fund Bonds	353,900
Total Bonds	$803,900

Chapter X

SALE AND AWARD

Actual operation one of bargain and sale.—While money is borrowed by the municipality and in contemplation of law its bonds issued to evidence the loan, the actual operation is that of bargain and sale. Express statutory authority to issue bonds implies the power to sell them in the ordinary and usual manner; and the municipality may, by virtue thereof, sell the bonds and use the proceeds for the purpose intended, that being the mode most generally adopted in similar cases.[1]

Private sale.—A private sale of bonds as distinguished from a public sale means substantially that the municipality is not required to give public notice of an intended sale nor to ask for competing offers or bids. Ordinarily we find private sale forbidden by statute (because public sale is required) but permitted in certain cases. When it is not expressly forbidden it is permissible. As to short-term paper, public sale is not ordinarily required. The advantage of private sale to the municipality is that it may act promptly when market conditions are favourable. The advantage to the broker is obviously lack of competition and because of this a larger prospective profit. The disadvantage to the municipality is the possibility of an unconscionable bargain, because of the ignorance of public officials. While actual fraud is seldom practiced, it is obvious that an alert buyer, fully informed of market conditions, is apt to have municipal officials at a decided disadvantage. There are no disadvantages to the broker in a private sale.

Public sale.—Public sale of long-term securities is required by most statutes. A public sale is one of which public notice is required by advertising. It is advantageous to the municipality because free competition is more apt to result in the offer of the market price. The fact that there is competition

[1] Dillon, p. 1398.

and publicity is a protection to municipal officials both against fraud and unconscionable bargains and against their own credulity or lack of information.

Bidders may be requested to submit propositions for the purchase of the bonds:

(a) Naming the price which they will pay for the entire issue, in which case the award will be to the bidder offering the most money.

(b) Naming the lowest interest rate at which they will take the issue, in which case a bidder who will take 4½% bonds will secure the award in preference to other bidders who offer to take 4¾% bonds. A variation of this plan is to ask for bids at the lowest interest rate plus the greatest premium, (generally the price above par one hundred), bid must be very carefully studied and particular care taken to see that the offer complies with its terms.

(c) Naming the least amount of bonds the bidder will take and pay therefor the amount necessary to be raised and a premium in addition. This form of bid is discussed later.

Disadvantages of a public sale.—A public sale has its disadvantages. The period of advertising the notice of sale is ordinarily too long. To secure needed publicity, a week or more must elapse between the public offering and the receipt of bids, and the award. The lapse of time may result in the loss of an advantageous market. It may also work the other way. In determining the proposed interest rate, a forecast must be made of the market conditions likely to obtain at and after the time of sale. In 1920 a very large offering by an eastern municipality was being advertised just as the Bolshevist army threatened to enter Warsaw. By the day of sale the threatened danger to Warsaw had passed and the ensuing feeling of optimism resulted in a premium so large that as it turned out the bonds would have sold at a lower interest rate.

Public notice.—Where public notice is required, a mistake in advertising may make the sale irregular. Re-advertising must follow the statutory course. Thus an advantageous market may be lost.

The New York statute governing public sale.—The New York statute governing public sale is typical of the provisions found in most jurisdictions. "All bonds hereafter issued by any municipal corporation, or by any school district or civil

division of the State, shall be sold, in the case of a city of the first class as required by its charter or by any special act under which such bonds are issued, in the case of a city of the second class as required by section sixty-one of the second class cities law, and in all other cases at public sale not less than five or more than thirty days after a notice of such sale, stating the amount, date, maturity and rate of interest, has been published at least once in the official paper or papers, if any, of any such municipality, provided that if there is no official paper, then such notice of sale shall be published in a newspaper published in the county in which such bonds are to be issued, or a copy thereof shall be sent to and published in a financial newspaper published and circulating in New York City." [2]

The New Jersey plan.—New Jersey has evolved a plan peculiarly its own. It has been observed by students of municipal finance that municipalities have not always applied the premium, the price above par (generally one hundred) bid for the bonds, to the purpose for which the bonds are issued. Instances of gross abuse have been common. Some years ago, a New York city, desiring to obtain money for current expenses, refunded a large amount of its debt and deliberately made the interest rate much higher than market conditions required. A large premium resulted, and instead of being applied to the purpose for which the bonds were issued or placed in the sinking fund, this premium found its way into the municipal till and was used for current expenses. To prevent this sort of thing, the New Jersey statute [3] now provides that the notice of sale must state the amount of money necessary to be raised. The bidder is required to state the number of bonds he will take, bidding therefor the amount of money necessary to be raised and an additional sum of less than one thousand dollars. Suppose, for instance, that one hundred bonds of one thousand dollars each are offered for sale and the amount of money required to be raised is one hundred thousand dollars. A bidder may offer to pay one hundred thousand nine hundred dollars and to take therefor ninety-nine bonds. This plan has worked advantageously in practice and has resulted in abolishing premiums of more than nominal amounts.

[2] Cons. Laws, Chap. 24, Sec. 9.
[3] P. L. 1917, p. 803, as amended.

Par means the amount of the face of the bonds and accrued interest from the date of the bonds to the date of delivery. Most statutes require that sales be made at not less than par. It is clear that unless a controlling statute provides to the contrary, a municipal bond may be sold at any price not so low as to make the sale usurious.[4]

Persons purchasing the bonds from the municipality are bound to take notice of the power of the municipality in this respect, and a sale of bonds at less than par is absolutely void between the parties if expressly prohibited by law. Neither party to the contract is bound thereby, and it cannot be the subject of a valid claim by either against the other.[5] If the bonds are paid for and in the hands of the original purchaser, the court would compel their surrender and provide for a refund of the purchase price. Note, however, that this is true only as between the parties. Our old friend the bona fide holder for value and without notice is protected if the bond is in fact a negotiable instrument and the municipality has the power to issue it.

Par sale.—Par sale requirements seem to involve an economic fallacy. Money is a commodity and the price of money is governed by the conditions existing at the time it is bought. It may be said that the interest rate borne by the bonds and the market rate never correspond. It is, therefore, necessary, to be sure of obtaining bids, to fix the interest rate higher than the market. The bonds may then sell for a premium. Theoretically, if the premium is properly applied, that is, paid into a sinking fund and properly invested, it reduces the interest rate to the market rate. In practice, this rarely happens. Par sales statutes are designed to compel the payment of a fair price for bonds and possibly to protect the reputation of municipal officials against charges of making bad bargains or fraudulent bargains. Sale after public notice does undoubtedly prevent intentional or unintentional abuse of power by public officials.

Evasion of such requirements.—During the early part of the year 1921, many smaller municipalities found it difficult to sell their shorter-term bonds at a six per cent interest rate, the highest rate permitted by statute. Most eastern statutes, and probably most bond acts, prescribe a maximum interest

[4] *Kiernan v. City of Portland* (Ore. 1912), 122 Pac. 764.
[5] Dillon, p. 1400.

rate of six per cent. If a six per cent bond is not worth par and the municipality cannot legally pay more than six per cent, the irresistible force of market conditions meets the immovable wall of statute, without, however, always producing an *impasse*. In other words, par sale statutes are frequently evaded.

Fiscal agency contracts.—These are popular in some parts of the country. By fiscal agency contract is not meant the bona fide contract whereby a banking institution acts as the disbursing agent for interest and principal, the bank sometimes acting as depositary,[6] but substantially that the bond house offers, for a consideration, to buy the bonds at a certain price at private sale or to bid not less than a certain price at public sale, to furnish all legal advice necessary in connection with the issue and to prepare the printed bonds for execution. This is substantially what is known in some parts of the country as a proceedings contract, by which the bond house offers certain services and receives a lump sum sufficient to permit it to make a reasonable, or sometimes unreasonable, profit on the bonds at the highest interest rate permitted by law. The legality of such contracts is at least questionable.

The deposit agreement.—As a method of evasion of par statutes, the deposit agreement has come into vogue within recent years. This form of contract includes an agreement to deposit the purchase price of the bonds with or in a particular depositary or to permit the purchaser to retain the purchase money and pay it over at fixed times in the future or upon request. The advantage derived is that the purchaser obtains the interest earned by the deposited purchase price, either in gross or in part, for such time as the deposit remains.

The legality of such an agreement may turn on whether the purchaser is or is not a proper depositary for municipal funds, as a bank in the same State would be ordinarily. If the purchaser is a depositary bank and the fund may be withdrawn at any time and before withdrawal earns interest as other municipal funds, the deposit is lawful. If the agreement is that the fund remain for a specified period, or earn less than usual interest, then either the sale is a sale on credit and void for that reason[7] or the provision of this agreement

[6] Chamberlain, p. 519.

[7] *Illinois v. Delafield* (1840), 8 Paige (N. Y.) 526.

that the fund is not to be withdrawn is unenforceable. If the purchaser is not a depositary and cannot qualify as such, because of statutory or other restrictions, the agreement is void as a sale on credit.[8] In any event, these questions can affect only the immediate parties to the transaction, i.e., the municipal officials and the purchasing bond house. The purchaser without notice takes title free from infirmities in the contract of sale.

Meeting the expense of issuing bonds.—Expenses incurred in issuing bonds may ordinarily be paid out of the proceeds of sale notwithstanding a prohibition of a sale below par,[9] but this depends on the statute pursuant to which the bonds are issued. The extent to which an allowance may be made to the purchaser for his expenses is not clear. Bona fide expenses incident to the issue of the bonds, such as printing and engraving, seem to be allowable. Allowance of other expenses including attorneys' fees is in doubt. If a claim for expenses is unreasonable in amount or is made a cloak for a deduction from the purchase price, it is clearly illegal.[10] If the expenses allowed the purchaser are legitimate, the payment of such expenses would probably be sustained but not if merely a device to effect a sale below par.

Brokerage and commissions.—These are allowable if bona fide but not if made a device to evade the statutory requirement of a par sale. The power of a municipality to issue and sell bonds carries with it the implied power to secure such reasonable and necessary assistance as may be requisite to bring about an advantageous sale, and to this end the municipality, acting in good faith, may employ a broker regularly engaged in the business.[11] This does not mean, however, that the bond house may be both the broker and the customer. The investment banker ordinarily buys for his own account, both ostensibly and in fact. If the bond house desires to act as a broker, disclose the name of its purchaser to the municipality, and have the award made to its customer, it can claim a reasonable brokerage. The difficulty is that the bond house is not willing to do this. There is some confusion in the decisions as to whether an agent may be employed only in an

[8] *Illinois v. Delafield* (1840), 8 Paige (N. Y.) 526.
[9] *LeRoy v. Elizabeth City* (N. C. 1914), 81 S. E. 1072; 166 N. C. 93.
[10] *Uhler v. City of Olympia* (Wash. 1915), 151 Pac. 117; 87 Wash. 1.
[11] Dillon, p. 1399.

emergency as where the bonds have been offered for sale at the highest permitted interest rate without finding a purchaser. It is contended, however, that an agent may be employed when his services are reasonably required. The question may be raised whether the commission of an agent should be paid from the proceeds of the bond issue or from some other available funds. There is considerable difference of opinion on this point but the question in theory seems only from which pocket the payment be made. Practically, the statute must be consulted.

In concluding this discussion of par sales or sales at less than par, it should be repeated that a sale of bonds at less than par, contrary to a statutory direction, does not affect the fundamental power of the municipality to make and issue the bonds; it is a mere irregularity in the exercise of its powers, and the validity of the bonds in the hands of innocent purchasers for value is not affected thereby.[12]

Plan of sale important to bidder and those in charge of sale.—The plan of sale determined upon should be carefully considered by the prospective bidder and the conditions upon which bids are canvassed should also be carefully studied by those in charge of the sale. The bid must be responsive to the advertisement. If it contains matter not properly responsive to the advertisement, it is usually a qualified bid and may be thrown out by the officials in charge of the sale.

Illustrations of notices of sale.—Illustrations of notices of sale in New York and New Jersey and the corresponding forms of bids follow this chapter.

[12] Dillon, p. 1401.

Notice of Sale of New York Union Free School District Bonds

NOTICE OF SALE
$245,000 SCHOOL BONDS
UNION FREE SCHOOL DISTRICT NO. 8
OF THE TOWN OF ORANGETOWN, NEW YORK

Sealed proposals will be received by The Board of Education of Union Free School District No. 8 of the Town of Orangetown, of the County of Rockland, New York, on October 4, 1921, at 8 P.M. o'clock at the Schoolhouse, Pearl River, New York, for the purchase of $245,000 School Bonds of said Board. Said bonds will be of the denomination of $500 each, will be dated November 1, 1921, and will mature:

$ 7,000 on November 1, 1922 to 1924
8,000 on November 1, 1925 and 1926
9,000 on November 1, 1927 and 1928
10,000 on November 1, 1929
11,000 on November 1, 1930 and 1931
12,000 on November 1, 1932
13,000 on November 1, 1933
14,000 on November 1, 1934
15,000 on November 1, 1935
16,000 on November 1, 1936
17,000 on November 1, 1937
18,000 on November 1, 1938 to 1940
17,000 on November 1, 1941.

Said bonds will bear interest at the rate of six per cent (6%) per annum, payable semi-annually on the first days of May and November in each year. Both principal and interest will be payable in lawful money of the United States of America at First National Bank of Pearl River, Pearl River, New York. The bonds will be coupon bonds, with the privilege of registration as to both principal and interest.

The right is reserved to reject all bids, and any bid not complying with the terms of this notice will be rejected.

The bonds will not be sold for less than par and in addition to the amount bid the successful bidder must pay accrued interest at the rate borne by the bonds from the date of the bonds to the date of payment of the purchase price.

All bidders are required to deposit a certified check payable to the order of said Board of Education for two per centum of the amount of bonds bid for, drawn upon an incorporated bank or trust company. Checks of unsuccessful bidders will be returned upon the award of the bonds. No interest will be allowed upon the amount of the check of a successful bidder and such check will be retained to be applied in part payment for the bonds or to secure the board against any loss resulting from the failure of the bidder to comply with the terms of his bid.

Proposals should be addressed to James B. Moore, Clerk of the Board of Education, Pearl River, New York, and enclosed in a sealed envelope marked on the outside "Proposal for Bonds."

The successful bidder will be furnished with the opinion of Messrs. of New York City, that the bonds are binding and legal obligations of the board.

The bonds will be prepared under the supervision of the United States Mortgage & Trust Company, which will certify as to the genuineness of the signatures of the officials and the seal impressed thereon.

By order of the Board of Education.
Dated, September 21, 1921.

JAMES B. MOORE,
Clerk of the Board of Education.

Form of Proposal for Such Bonds, Pursuant to the Foregoing Notice of Sale

PROPOSAL FOR BONDS

October , 1921.

BOARD OF EDUCATION,
Union Free School District No. 8,
In the Town of Orangetown, Pearl River, New York.

Sirs:

Subject to the provisions of the annexed notice of sale, which is made a part of this proposal, we offer to purchase the bonds of the issue described in such notice and we offer to pay therefor $

In addition to the amount above stated we will pay accrued interest at the rate borne by the bonds from the date of the bonds to the date of payment of the purchase price.

We enclose herewith certified check payable to the order of the Board of Education of U. F. S. D. No. 8 of the Town of Orangetown, in the sum of $, being 2% of the par value of the bonds bid for, which check is to be applied in accordance with the terms of said notice.

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Notice of Sale of Bonds of a New Jersey City

JERSEY CITY, NEW JERSEY

NOTICE OF SALE

$2,275,000 GENERAL IMPROVEMENT BONDS
$1,892,000 WATER BONDS

Sealed proposals will be received by the Director of the Department of Revenue and Finance of the City of Jersey City, New Jersey, on September 7, 1921, at 12 o'clock noon at the City Hall in said City for the purchase of the following issues of bonds, the amount of the issue stated in each case being

the authorized amount of bonds and the sum required to be obtained at the sale of such issue:

$2,275,000 General Improvement Bonds maturing $62,000 on September 1 in each of the years 1922 to 1939 inclusive, and $61,000 on September 1 in each of the years 1940 to 1958 inclusive.

$1,892,000 Water Bonds, maturing $49,000 on September 1 in each of the years 1922 to 1941 inclusive, and $48,000 on September 1 in each of the years 1942 to 1960 inclusive.

Said bonds will be dated September 1, 1921, will be of the denomination of $1000 each, will bear interest at the rate of five and one-half per centum (5½%) per annum, payable semi-annually on the first days of March and September in each year. Both principal and interest of said bonds will be payable in lawful money of the United States of America at the office of The Treasurer of said City. The bonds will be coupon bonds, with the privilege of registration as to principal only or as to both principal and interest.

No more bonds of each issue will be sold than will produce a sum equal to the authorized amount of such issue and an additional sum of less than $1000. Unless all bids are rejected, each of said issues will be sold to the bidder or bidders complying with the terms of sale and offering to pay not less than the sum required to be obtained at the sale of such issue, and to take therefor the least amount of bonds, commencing with the first maturity (stated in a multiple of $1000); and if two or more bidders offer to take the same amount of such bonds, then to the bidder or bidders offering to pay therefor the highest additional price. The right is reserved to reject all bids and any bid not complying with the terms of this notice will be rejected.

In addition to the amount bid the purchaser must pay accrued interest at the rate borne by the bonds from the date of the bonds to the date of payment of the purchase price.

Any bidder may condition his bid on the award to him of two or more of said issues but in that case if there is a more favorable bidder for any one of the issues for which he bids, his bid will be rejected.

All bidders are required to deposit a certified check payable to the order of The Treasurer of Jersey City, New Jersey, for two per centum of the amount of bonds bid for, drawn upon an incorporated bank or trust company. Checks of unsuccessful bidders will be returned upon the award of the bonds. No interest will be allowed upon the amount of the check of a successful bidder, and such check will be retained to be applied in part payment for the bonds or to secure the City against any loss resulting from the failure of the bidder to comply with the terms of his bid.

Proposals should be addressed to James F. Gannon, Jr., Commissioner of the Department of Revenue and Finance, Jersey City, New Jersey, and enclosed in a sealed envelope marked on the outside "Proposals for Bonds."

The successful bidder will be furnished with the opinion of Messrs. of New York City, that the bonds are binding and legal obligations of the City.

The bonds will be prepared under the supervision of the United States Mortgage & Trust Company, which will certify as to the genuineness of the signatures of the officials and the seal impressed thereon.

By order of the Board of Commissioners.
Dated, August 16, 1921. .....

Director of the Department of
Revenue and Finance.

Form of Proposal for Such Bonds, Pursuant to the Foregoing Notice of Sale

PROPOSAL FOR BONDS

Dated, , 19

Mr. James F. Gannon, Jr.,
Commissioner of the Department of Revenue and Finance,
Jersey City, New Jersey.

Sir:

Subject to the provisions of the annexed Notice of Sale, which is made a part of this Proposal, we offer to purchase bonds of the issues described in such notice, in the principal amounts stated below, the bonds bid for being those of each issue first to mature:

Of the $2,275,000 General Improvement Bonds

We offer to purchase $
We offer to pay therefor $

Of the $1,892,000 Water Bonds

We offer to purchase $
We offer to pay therefor $

In addition to the amounts above stated we will pay accrued interest at the rate borne by the bonds from the date of the bonds to the date of payment of the purchase price.

(The bidder must strike out one of these paragraphs.)

This bid is conditioned on the award to us, in accordance with this bid, of all or none of the bonds bid for.

This bid is a separate and distinct bid for each of the said issues, and any one of said issues may be awarded to us.

We enclose herewith certified check payable to the order of The Treasurer of Jersey City, New Jersey, in the sum of $ being two per centum (2%) of the par value of the bonds bid for which check is to be applied in accordance with such notice.

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Chapter XI

DEFAULT, AND REMEDY OF BONDHOLDERS

Default.—A very able lawyer once said to the writer that the real question involved in corporate and municipal financing was, "what happens if there is a default." The careful investment banker as well as the investor must have the consequences of default constantly in mind.

A default occurs when the interest on or the principal of a bond is not paid when due. It is of interest to note that default in the payment of interest on municipal bonds has no effect upon the maturity of the principal. Default in the payment of interest on a corporate bond generally makes the principal payable immediately. This is not so in the case of municipal bonds. A default in the payment of one coupon, or interest due on a specific date, does not make the principal payable nor does default in the payment of one or more serial bonds cause the remainder of the series to become due and payable.

Former cases of default.—A very large number of municipalities have defaulted in the payment of their bonds and other obligations, but such defaults are now comparatively infrequent. A list of 510 cases in which municipal bond issues have been held illegal, and in regard to which there was, it is to be presumed, a default, is contained in a book entitled, "Municipal Bonds Held Void," published in 1911 by Maurice B. Dean. In 249 of the cases in that list, the bonds were held void after they had been issued.

It would be very difficult to prepare a complete list of repudiations of municipal bonds, arising from financial incompetency or bad faith. A number of such defaults are referred to in Chamberlain,[1] Jordan[2] and Raymond.[3] In addition to the cases referred to by these authors, the following may be mentioned:

[1] Chamberlain, pp. 235, 236.
[2] Jordan, p. 83.
[3] Raymond, pp. 153, 156.

In 1872 the debt of the City of Watertown, Wisconsin, was $750,000, and the assessed valuation of its property was a little over $1,000,000, so that it was practically impossible for the city to pay its debt.[4]

In the years following 1876, the City of Elizabeth made extensive improvements, many of which were merely aids to real estate speculations, assessed the cost upon property benefited, and issued bonds against the assessments. The assessments were held to be invalid, and the debt was too great to be paid from the proceeds of general taxes. In 1879 the debt of the city was so large it would have required annual taxation at the rate of six per cent to meet the city's obligations for interest and current expenses.[5] It is gratifying to record that such indebtedness of this city has long since been adjusted and its bonds are now legal investments for savings banks and trustees in the State of New York.

The *Daily Bond Buyer* of August 29, 1921, prints the following:

"The City of Victor, Colorado, has been ordered by U. S. District Judge Robert E. Lewis of Denver to raise $38,000 by taxation to pay a judgment in favour of the First National Bank of Ithaca, N. Y. This judgment was obtained, it is stated, as a result of a suit brought to compel payment on bonds issued by the city in 1915 on which neither principal nor interest had been paid."

Reasons for default.—Reasons for default are the inability or the unwillingness of the municipality to pay its debts. Inability may follow a judgment of a court of competent jurisdiction declaring proceedings prior to issue irregular and the bonds invalid, in which case no tax can be levied to pay them.

A limited tax rate may exist, beyond which the municipality may not go, or there may have been a marked shrinkage in assessed valuation of taxable property. Repeating what has been said before as to the effect of a limited tax rate, it is obvious that if such a limit exists and the assessed valuation of taxable property remains fairly constant, a fixed amount of revenue will be derived each year. The municipality must live before its debts are paid, and in practically all jurisdictions (with the possible exception of Ohio), this is settled law. If there is not enough money left after the munici-

[4] *Rees v. City of Watertown* (1873), 19 Wall. 107 at 110.
[5] Dillon, p. 2512.

pality's running expenses are paid, to care for debt service, so much the worse for the bondholder.

Mr. Chester B. Masslich has the following to say about the effect of tax limits:

"It must be remembered that a tax limit which appears to be sufficient at the time of the issuance of a public security may presently become insufficient. Alabama has had exactly that experience. Assessed valuations change from year to year. Sometimes they change because property values have increased or decreased, but in many States they have changed by fiat of the legislature, which has established a different basis of taxation and a different ratio between actual values and assessed values. Investors are well acquainted with the fact that these changes have sometimes been made on a downward scale. In Kentucky, where a constitutional limitation of bond taxes still prevails, a school district issued a comparatively small amount of bonds when its assessed valuation was about $1,500,000. Long before those bonds fell due, it became unprofitable further to develop the natural resources that had given the district its prosperity, and the assessed valuation fell to about $375,000. The 50-cent tax rate allowed by the State constitution would no longer produce the amount necessary to pay the interest and provide for a sinking fund, and the bondholders were compelled to compromise. Many such illustrations can be given in many States. In one prosperous Alabama city, where no question was raised as to the legality of any bonds it had issued, the authorities were able to effect a compromise which gave the bondholders new bonds at half the face value of the outstanding bonds and at only 3 per cent interest. Only one bond issue of that city escaped the general disaster, through the fact that it constituted a lien upon public property, and the bondholders took possession of that property under order of the United States courts. * * *

"There are communities in the United States, which, abhorring the very thought of repudiation, have nevertheless been compelled to repudiate and compromise because the maximum limits of taxes they were permitted to levy have not been sufficient to meet their debts. One of the greatest American cities suffered this dishonour, but rose in its might and demanded and obtained a constitutional amendment for itself alone, empowering it to levy sufficient taxes to pay its

creditors. It was many years, however, before it could outlive the effects of that dishonour. The laws permitting investment of funds of savings banks in New York and the various New England States, make it a condition of such investments that no default shall have occurred within a given long period. Investors remember these defaults. They are sensible of the reasons why the defaults occurred and they are not anxious again to put themselves into a position which makes the payment of their bonds dependent upon the continued prosperity of the city or county which issued them." [6]

Shrinkage of assessed valuation is by no means unknown. The fiscal history of the mining towns of the Rocky Mountain region is familiar to most students of municipal finance. Representatives of St. Michel de Laval, Quebec, reported to the proper provincial authority that the assessed valuation of the taxable property had shrunk in a few years from nearly $9,000,000 to a little over $2,000,000, and that the municipality had a debt of $2,500,000.

Bad faith.—Unwillingness to pay may result from various causes. Pomeroy, Ohio, in 1910, defaulted on its largest issue of refunding 6s. The reason ascribed was, that the bonds were not callable; but the village fathers felt they would like to retire the bonds, and took this means of accomplishing their purpose.[7] Unwillingness to pay almost invariably involves bad faith. In the cases where the proceeds of the bond issue have never been received by the municipality, but remain in the pockets of unscrupulous promoters or defaulting officials, it is difficult not to have some sympathy with the taxpayer.

To sum up, a recent writer, discussing defenses to actions brought to enforce the payment of municipal bonds, has the following to say:

"Absence of legal authority for the issuance of such obligations at the time of their issuance is always available, as a defense, except in case of legislative ratification; but there can be no such ratification if any constitutional provision would be thereby violated. Fraud or other official misconduct or delinquency in the issuance of the bonds, under an existing legal authority, or an excessive issue, or misapplication of the

[6] The *Daily Bond Buyer,* December 5, 1921, quoting from an article by Mr. Masslich in *Good Roads.*

[7] Chamberlain, p. 235.

bonds, or of their proceeds to an illegal or unauthorized purpose, or improper execution of the bonds, or other irregularities or omissions in the statutory requirements, may or may not be available as defenses, depending upon the facts and circumstances of the cases as they arise." [8]

The remedy of the bondholder.—Under the title, "Settling a Default in the Pioneer Days," a financial newspaper prints the following:

"Defaults of some western municipalities recall former difficulties that have been experienced in the history of Canadian municipal finance. Perhaps the most dramatic settlement between a group of bondholders and a defaulting municipality was arranged about thirty years ago between Portage la Prairie and an agent who was sent out to interview the city when it failed to meet its interest payments.

"When the agent arrived, a meeting of the townspeople was called. He asked them what they intended to do about paying their debts. The mayor of the town replied that the civic treasury was empty and the debts could not be paid at the moment.

" 'If you do not meet your debenture payments at once, you will get a sheriff's order to seize every building in town,' was the ultimatum of the financial man.

"The mayor and the leading townspeople held a hurried consultation. The mayor announced to the agent: 'Go to it, old boy. Get your sheriff's order. But we warn you that before you have had time to put it into execution we will organize the biggest moving bee that has ever been seen on the prairies. We'll drag every building in town over to the next townsite, change the name of the town, and let you have what's left.'

"A settlement was hastily arranged, the town's debts being consolidated and extended over a term of years. That was civic finance in the early days of the wild West." [9]

In ascertaining the rights and remedies of municipal creditors, special reference must always be had to the legislation pursuant to which the debts were created. If the legislature authorizes the creation of a debt and provides no special mode for its payment, it is a sound proposition that it was intended that it should be paid in the usual way in

[8] Harris, "The Law Governing Municipal Bonds," p. 279.
[9] The *Daily Bond Buyer,* June 4, 1921.

which such debts are paid, viz., by the levy and collection of a tax for that purpose, if there is nothing to rebut such intention.[10]

We have seen that the powers of municipalities are derived from statutes and that such statutes must be carefully construed. Hence, it is necessary when we consider the enforcement of a municipality's contract liability, to pay careful attention to the legislation authorizing it, and especially to legislation intended to provide means to meet the obligation. It must also be remembered that the right to issue bonds is not the normal means of raising money. The normal method is the levying and collection of taxes.

Bonds are not liens. Seldom does a city bond have a prior lien upon, nor is it secured by any definite property. Statements on the part of over-enthusiastic bond salesmen to the effect that city bonds are secured by a prior lien upon all the property of the city, are far from the truth. In no part of the country except New England does possible default in payment even suggest the attachment of property. Municipal bonds are rarely secured by a mortgage of specific property; no instance of such security for eastern municipal bonds occurs to the writer.

Creditors must be paid from the proceeds of taxes. If municipal officials will not or cannot levy taxes in sufficient amount to pay the creditors of the municipality, the aid of the courts must be sought. The proper proceeding by the creditor is to apply to the court having jurisdiction, usually a Federal court, for a *writ of mandamus,* addressed to the municipal authorities, directing them to levy and collect a sufficient tax to pay the claim. A writ of mandamus is in substance an order or direction of the court to compel the performance of ministerial functions by officials who have no discretion to refuse to act in the manner directed. The courts will not direct that such a writ be issued if there is a plain and complete remedy by the ordinary process of the law, and it has, therefore, been generally held that if the creditor brings suit against the corporation, and obtains a judgment for a sum of money, the writ of mandamus will not be issued to compel payment. This holds true only when there is some other way of enforcing and rendering the judgment effectual.[11]

[10] Dillon, p. 2688.
[11] Dillon, p. 2677.

Judgments must be obtained.—Ordinarily, the municipal creditor must obtain a judgment which conclusively establishes the amount due him.[12] This is the practice in the Federal courts. When the sheriff or corresponding proper officer says that there is no property which he can attach or secure to satisfy the judgment, then a writ of mandamus may be issued. There is no necessity for obtaining a prior judgment if the bondholder, according to the statute, is expressly entitled to a levy of a special tax to pay his bond. If the duty of levying it has been neglected or refused, it is not necessary that an execution should in such case be secured and returned unsatisfied, in order to entitle the judgment creditor to a writ of mandamus.[13] When the claim is reduced to judgment, the duty to provide for its payment becomes perfect, and if the claim can be paid in no other way, it must be met by the levy and collection of a sufficient tax for that purpose. As has been said, this duty will be enforced by the courts.[14] If the order of the court is not obeyed, the delinquent officials may be, and in many cases have been, committed to jail for contempt of court.

Effect of limited tax rate.—The courts will not enlarge the statutory powers of the municipal officials to levy taxes. If there be a limited tax rate the municipal officials may be ordered to tax the limit permitted by law, but may not be ordered to exceed it. This is true where the limit applies to a special or particular tax for the payment of the bonds, or where it applies to all municipal levies to provide funds for the running expenses and debt service of the municipality. The courts will not legislate for the bondholder.

Contracts with the bondholder.—The statutes authorizing the issue and the levy of taxes for the payment of bonds are parts of the contract between the municipality and its bondholders. Hence the courts will grant writs of mandamus to compel the levy of taxes to the full limit in force when the debt was created, although a subsequent constitutional restriction on the amount of taxes which may be levied has become operative.[15] The Federal Constitution prohibits impairment of contracts.

[12] Dillon, p. 2690.
[13] Dillon, p. 2691.
[14] Dillon, p. 2679.
[15] Dillon, p. 2685, note.

Actions based upon the contract evidenced by the bond may in some cases be brought by the bondholders. A municipal corporation may be sued if it fails to perform its contracts, upon a contract within the scope of the powers of the corporation and duly entered into by the proper officers as agents. Municipal corporations are liable in the same manner and to the same extent as private corporations or natural persons. They are not liable on contracts beyond their powers or bound by contracts by unauthorized officers or agents.[16]

Municipal corporations are likewise liable to actions on implied contract. So a bona fide purchaser of a city's bonds, which are apparently valid but which are wholly void may, it has been held by the courts, recover the money paid for the bonds. The cases on the implied liability of municipal corporations "run on nice lines of distinction" and turn on the constitutional and statutory provisions involved and the facts.[17] It is not possible to generalize, and it must be remembered that even though a judgment be recovered, the judgment must be paid from the proceeds of taxation. If the power to tax is limited, a judgment may be uncollectable.

The question is sometimes asked whether receivers can be appointed in the case of defaulting municipal corporations. They cannot be. The appointment of the receiver is an equitable remedy, and equitable remedies are given by the court only when the legal remedy is inadequate. As has been pointed out, the remedy of the bondholder in case of default is to obtain a judgment and obtain an order of the court, called a *writ of mandamus,* directing the proper officials to levy a sufficient tax to pay the bond. If a sufficient tax cannot be levied because of limitations, the bondholder is out of luck. The operation to enforce the order of the court directing municipal officials to collect sufficient taxes does not need the aid of a receiver. Furthermore, municipal bonds are not liens upon municipal properties, that is, the public buildings, water and sewer systems, parks and lands owned by the issuing political unit. Hence the income from such properties cannot be applied to debt service except to the extent that the income may, pursuant to proper statutory authority, be pledged in advance to the payment of the bonds. The author

[16] Dillon, pp. 2810–11.
[17] Dillon, pp. 2823–24 and note.

knows of no case in this country where a receiver has been appointed, although applications have been made in a few instances for the appointment of a receiver. It is probably true that in Canada it is possible under existing legislation for the provincial authorities to step in and administer the affairs of a defaulting municipality, but this is only because of the statute authorizing such procedure. Admirable as this provision may be, the idea of such direct intervention is not in accord with American ideas of municipal and State government.

Legislative relief.—Legislative relief is sometimes accorded the bondholder, but the claim and the debt may not be such as the law recognizes as a legal obligation. It is possible for the legislature to compel municipal corporations to recognize debts or claims, not binding in strict law, which for technical reasons cannot be otherwise enforced, but which nevertheless are just and equitable in their character, and involve a moral obligation.[18] Constitutional limitations, whether they be limitations on the tax rate or the amount of debt to be incurred, cannot be brushed aside by legislatures, and if such restrictions prevent payment, legislatures are powerless to afford relief.

But when all is said and done, there can be no further assurance of good faith given investors in municipal bonds than the simple statement that no American municipality of any importance has defaulted in recent years on the principal or interest of any of its obligations.[19]

[18] Dillon, p. 222.
[19] Chamberlain, p. 23.

Chapter XII

BONDS AS INVESTMENTS

Definition.—To make an investment, implies divesting one's self of the possession and control of one's assets and granting such possession and control to another. Stated in more specific language, we mean that when we make an investment, we take our money and turn it over to somebody else in return for a promise to repay the money loaned and to pay interest for the use of the money so paid over. The word "loan" is the practical equivalent.

In common parlance, a purchase of stock is called an investment, but it is not really an investment because there is no promise that the money used will be returned at a stated time. A person who buys stock and becomes a stockholder becomes a joint adventurer; he is not a creditor. A partner in a business concern may contribute a part of the capital employed in the business, and he is not, under ordinary conditions, a creditor. His right to withdraw his contribution is, therefore, always subject to the prior right of other creditors who have extended credit to the partnership. Consequently, in the sense in which we are using the term, a partner is not an investor.

On the other hand, a purchaser of securities which are ordinarily regarded as the proper media for investment, may be a speculator. Such a purchaser takes the interest earned as an incident, but expects that his profit will come from a rise in value of the security. Speculation and investment are actuated by the same motive: desire for gain, and the difference between them is the difference in degree of risk the individual is willing to assume. It is ordinarily true that the greater the return upon an amount invested or adventured, the greater possibility there is that the principal may be lost. Conversely, the greater the certainty is that the principal will be returned, in accord with the promise, the smaller the return will be.

The ideal investment.—An ideal investment is described by Chamberlain [1] as follows: "If an investor has obtained (1) security for his principal, (2) a fixed or definite interest, (3) a fair return in income, and (4) an investment which is salable without difficulty, and (5) is acceptable as collateral, and (6) is free from direct tax, and (7) requires almost no care, and (8) matures after a satisfactory lapse of time, and (9) is in convenient units of denomination, and (10) has as good a chance of appreciating as of depreciating as its qualities become more generally recognized,—that man is to be felicitated."

This author also says: "that any investment which will measure up to the standard of these qualities mentioned is well-nigh ideal."

Municipal bonds as ideal investment.—Municipal bonds possess all of the characteristics of a good investment, except the possible factor of appreciation in value as maturity is approached. A bond purchased at a discount from par will appreciate in value as maturity approaches, but a premium bond depreciates, although market conditions may increase its value for a period.

Applying the tests of a good investment to municipal bonds and at the same time defining our terms we find:

Security of principal.—This means that, within the bounds of reason, the principal will be returned to the lender at the time agreed upon or that it can be converted at will or at a fixed time into some equivalent form of wealth, equal in value and equally satisfactory to the lender. Municipal bonds are due and payable at an agreed time, and although as we have seen, there have been municipal defaults (and the possibility of such default ought always to be in the mind of the investment banker and the bond buyer), the percentage of such defaults is very low indeed.

Stability of income.—The municipal bond bears interest at a fixed rate per cent ordinarily payable semi-annually. The amount received on each of the semi-annual interest dates is the same and is not subject to abatement or fluctuation. It is paid at regular intervals in predetermined amounts. The interest on municipal bonds is ordinarily paid promptly, for municipal credit depends to a large extent upon promptness. A coupon, when detached and cancelled, is a promise, inde-

[1] Chamberlain, pp. 27–28.

pendent of the promise of the bond, to pay the amount of money called for.

Fair income return.—The question as to what constitutes a fair return on the income invested, depends upon many factors. All other things being equal, the income return varies inversely as the security. When the factor of safety is considered, the income return on the average municipal bond (which may be greater or less than the coupon or stated interest rate) will be found to be in very close accord with the market value of money.

Marketability.—By this we mean salability without loss of time hunting for a purchaser. We mean something which has a ready market; which can be quickly sold and converted into money. The Koh-i-noor and the Cullinan diamonds possess great value, but neither stone is marketable because of its enormous value and the limited number of people who could afford to buy it. To be marketable, then, the selling price of a commodity must be such as not to be prohibitive, and the demand must be more or less constant. It is a fact that municipal bonds possess a very high degree of marketability.

Tax exemption.—In the last analysis, all wealth is taxed, and it is a question only of the directness of its imposition: of the incidence of taxation, as the economists say. But the incidence of taxation is so unequal that one may often profit by knowledge of the working of this unequality, or at least he may secure his investment from unforeseen levies by the provisions of his investment contract, or by taking advantage of the provisions of statutory law. We will consider tax exemption more in detail later on. It is sufficient to say at this point that the municipal bond is ordinarily tax-exempt in the State of issue, and always exempt from Federal impositions.

Exemption from care.—Funds on deposit are subject to changing rates of interest. Mortgages require attention to many details, such as verification of the payment of taxes and care that repairs are made to avoid depreciation of the mortgaged property. Real estate requires constant attention, for the collection of rents, the making of repairs and alterations, and betterments for tenants. A bond which is registered as to principal and interest, on which the owner receives the interest by check at stated periods, or from which he may detach the coupons and cash them, requires little care. A safe

deposit box for the registered bond, and semi-annual visits to it in the case of the coupon bond, represent all the care that is necessary for the bond if the bond has been wisely selected in every respect.

Acceptable duration.—The investor, if an individual, does not care particularly about changing the character of his investments, and prefers that they remain constant for periods of shorter or greater duration. Investments for individuals may be said to be for a lifetime. Where no question of depreciation of security is involved, a term of from twenty to fifty years is not too long, and it is generally true that investors prefer the longer- to the shorter-term bond. Trustees and executors have particular requirements which depend upon the terms of the trusts pursuant to which they are acting. While the tendency has been to shorten the term of municipal bonds, and while new issues of municipal bonds rarely have an average term of more than twenty years, it is possible for any kind of an investor to select a bond having a term which meets his particular needs.

Acceptable denomination.—Municipal bonds are ordinarily of the denomination of $1,000 each, although there are many bonds of smaller denominations (called "baby bonds") offered in the market from time to time. The denomination of $1,000 is an easy one in which to make computations and is the accepted denomination in the market.

Potential appreciation.—By this we mean possible increase in value of the principal. The possibilities of appreciation in speculation are without limit, but such appreciation is a desirable, although not a necessary, incident of a good investment. Property secured by a mortgage is apt to depreciate in value unless current repairs are promptly made. Obsolescence, by which is meant a change in mode of operation which renders changes necessary in buildings or machinery, may destroy the security. Obsolescence is not a factor as to municipal bonds, being cared for by serial payments of principal or the accumulation of a sinking fund.

If the value of the bond increases, so much the better for the bondholder. If a bond is purchased at a discount, more than the purchase price is returned at maturity; hence it appreciates. If it is purchased at a premium, less is returned; hence it depreciates in value. It is therefore obvious that any bond, municipal or corporate, cannot much appreciate, and as

its maturity date draws near, its value approaches par. For a more adequate treatment of this subject, the student is referred to the admirable discussion in Professor Jordan's work on "Investments," entitled "Mathematics of Investments."

Investments by fiduciaries.—Trustees and executors of estates, guardians of minor children, and committees for incompetent persons, are held to a very strict accountability for the funds entrusted to their care and management. It has seemed wise to the lawmakers of many States specifically to define the kind of investments which such fiduciaries can make. A reference to the statutes of all the States is not possible here, but the general principles may be inferred from an examination of the statutes of New York. While such statutory regulations are intended to secure trust funds against loss, it must be remembered that the test of the character of investment is entirely within the judgment of the legislatures of the various States, and their requirements may appear to be arbitrary, but the legislatures are the judges.

Savings banks in New York may invest the moneys deposited therein in the following securities, among others:

(a) The stocks, bonds, interest-bearing obligations or revenue notes sold at a discount, of any city, county, town, village, school district, union free-school district or poor district in New York State, provided that they were issued pursuant to law and that the faith and credit of the municipality or district that issued them is pledged for their payment.

(b) The stocks or bonds of any incorporated city, county, village or town situated in one of the States which adjoins the State of New York, if its indebtedness together with the indebtedness of any district or other municipal corporation or subdivision, except the county included therein, less its water debt and sinking fund, is seven per cent or less of its assessed valuation. The bonds of counties are legal investments if their indebtedness less sinking funds is within seven per cent of the taxable property.

(c) The stocks or bonds of any incorporated city, situated in other of the States of the United States which were admitted to statehood prior to January, 1896, and which since January, 1861, has not defaulted, provided such city has a population of not less than 45,000 inhabitants, has been incorporated at least twenty-five years, and has not, since January 1, 1878, defaulted for more than ninety days in the

payment of principal or interest of its indebtedness, or effected any compromise with the holders thereof. If the indebtedness of such city has been paid, refunded or compromised, then a new period as to default begins to run. The limitation on indebtedness, which must include any district, other municipal corporation or subdivision, except a county, wholly or partly included therein, less its water debt and sinking funds, may not exceed seven per cent.[2]

Fiduciaries may invest in any security in which a savings bank may invest its funds.[3]

The New York State superintendent of banks each year issues a list of cities, counties, etc., the bonds of which are "legal investments," having made during the preceding year an examination of the facts upon which such list is predicated. The fact that the name of any particular municipality is omitted, does not necessarily mean its bonds are not legal, but may mean its financial officials have been negligent in supplying requested data. A list of "legals" in New York, Massachusetts and Connecticut follows this chapter.

After a bond has been purchased by a bank, and for some reason the situation changes so that the bond ceases to meet the legal requirements, must the bank sell the bond? The Attorney General of New York has decided that a savings bank may be compelled to do so by the State banking superintendent.[4]

It is probably true that the ordinary trustee would be accountable to his beneficiaries if a bond, having ceased to be a legal investment, should depreciate in price.

Postal savings deposits.—Under the Postal Savings Law the funds received at postal savings depository offices of each city, town, village or other locality, must be deposited in solvent banks located therein, provided these banks qualify to receive deposits. One of the qualifications is the pledging by the banks against the deposits, of such securities as the board prescribes. The Board of Trustees by its regulations of August 16, 1916 (as amended) has prescribed the terms and conditions of the figures at which different classes of municipal bonds will be accepted.

Bonds of any city or county having a population of over

[2] Cons. Laws, Chap. 2, Sec. 239.
[3] Cons. Laws, Chap. 13, Sec. 111; Chap. 14, Sec. 85; Chap. 50, Sec. 116.
[4] Opinions of Attorney General, 1908, p. 371.

30,000 are accepted at 90 per cent of their market value, but if such market value is above par, they will be accepted at only 90 per cent of the par value; bonds of any city, town, borough or village of the United States having a population of between 20,000 and 30,000 are accepted at 80 per cent of their market value, provided said market value is not in excess of par; while bonds of any other city, town, county or other legally constituted municipality or district of the United States, otherwise eligible, are accepted at 75 per cent of their market value but not to exceed 75 per cent of the par value. Bonds of school districts are included in this classification.

The regulations further provide that the municipality or district must have been in existence for a period of ten years, must not have defaulted for ten years and must not have a net funded indebtedness exceeding 10 per cent of the valuation of its taxable property. The regulations have further defined "net funded indebtedness." The definition is interesting for the reason that the bonds of any civil division, whose territorial limits are approximately coterminus with the municipality or district, must be included in computing gross debt. Sinking funds, bonds or obligations payable from current revenues, and bonds issued to provide public utilities, if self-sustaining, assessment bonds to the extent that these bonds are secured by uncollected assessments, and bonds which are to be paid from funds given by the State, may be deducted in determining the net debt. To be eligible, the bonds must be general obligations, payable without limitation to a special fund, from the proceeds of taxes levied upon all the taxable, real, and personal property within the territorial limits of the issuing municipality or district. Revenue bonds, temporary bonds, temporary notes, certificates of indebtedness and warrants are excluded. Provision is made for bonds of consolidated or merged municipalities.[5]

[5] State and City Section of the *Commercial and Financial Chronicle,* December 25, 1920.

State and City Bonds Legal for Savings Banks in New York, Massachusetts, and Connecticut

(Supplement to THE BOND BUYER of New York, September 24, 1921.)

(According to the latest lists issued by the State Banking Departments of New York, Massachusetts and Connecticut.)

Key: NY = New York M = Massachusetts Ct = Connecticut Revised to 9/14/21

Bonds of	Legal in			Bonds of	Legal in			Bonds of	Legal in		
Akron, Ohio	NY	M	Ct	Bayonne, N. J.	NY	..	Ct	California	NY	M	Ct
Alabama	NY	..	..	Beaumont, Tex.	...	..	Ct	Cambridge, Mass.	NY	M	Ct
Alameda, Cal.	...	..	Ct	Belleville, Ill.	...	..	Ct	Camden, N. J.	NY	M	Ct
Albany, N. Y.	NY	M	Ct	Bellingham, Wash.	...	..	Ct	Canton, Ohio	NY	M	Ct
Allentown, Pa.	NY	M	Ct	Beloit, Wis.	...	..	Ct	Cedar Rapids, Ia.	NY	M	Ct
Alliance, Ohio	...	..	Ct	Berkeley, Cal.	...	..	Ct	Charleston, W. Va.	...	..	Ct
Altoona, Pa.	NY	M	Ct	Beverly, Mass.	NY	M	Ct	Chelsea, Mass.	NY	M	Ct
Amsterdam, N. Y.	NY	M	Ct	Binghamton, N. Y.	NY	M	Ct	Chester, Pa.	...	M	Ct
Anderson, Ind.	...	..	Ct	Bloomington, Ill.	...	..	Ct	Chicago, Ill.	NY	M	Ct
Arizona	NY	..	..	Bloomfield, N. J.	NY	..	..	Chicopee, Mass.	NY	M	Ct
Arkansas	NY	..	..	Bluefield, W. Va.	...	..	Ct	Cincinnati, Ohio	NY	..	Ct
Ashtabula, Ohio	...	..	Ct	Boston, Mass.	NY	M	Ct	Cleveland, Ohio	NY	M	Ct
Atlantic City, N. J.	NY	..	Ct	Bridgeport, Conn.	NY	M	Ct	Clifton, N. J.	NY	..	..
Auburn, N. Y.	NY	M	Ct	Bristol, Conn.	NY	..	Ct	Clinton, Ia.	...	..	Ct
Aurora, Ill.	...	..	Ct	Brockton, Mass.	NY	M	Ct	Cohoes, N. Y.	NY	..	Ct
Baltimore, Md.	NY	M	Ct	Brookline, Mass.	NY	M	..	Colorado	NY	..	Ct
Bangor, Maine	...	M	Ct	Buffalo, N. Y.	NY	M	Ct	Colorado Springs, Colo.	...	..	Ct
Bath, Maine	...	M	..	Burlington, Ia.	...	..	Ct	Columbus, Ohio	NY	M	Ct
Battle Creek, Mich.	...	M	Ct	Burlington, Vt.	NY	M	Ct	Concord, N. H.	...	M	Ct
Bay City, Mich.	NY	M	Ct	Butte, Mont.	...	..	Ct	Connecticut	NY	M	Ct

Bonds of	Legal in		
Council Bluffs, Ia.	...	M	Ct
Covington, Ky.	NY	..	Ct
Cranston, R. I.	NY	M	Ct
Cumberland, Md.	...	..	Ct
Dallas, Tex.	NY	..	Ct
Danbury, Conn.	NY	M	Ct
Danville, Ill.	...	M	Ct
Davenport, Ia.	NY	M	Ct
Dayton, Ohio	NY	M	Ct
Decatur, Ill.	...	M	Ct
Delaware	NY	M	Ct
Denver, Colo.	...	..	Ct
Des Moines, Ia.	NY	M	Ct
Detroit, Mich.	NY	M	Ct
District of Columbia	NY	M	Ct
Dubuque, Ia.	...	M	Ct
Duluth, Minn.	NY	M	Ct
East Chicago, Ind.	...	..	Ct
East Liverpool, Ohio	...	..	Ct
Easton, Pa.	NY	M	Ct
East Orange, N. J.	NY	..	..
East Providence, R. I.	NY	M*	..
East St. Louis, Ill.	...	..	Ct
Eau Claire, Wis.	...	..	Ct
Elgin, Ill.	...	..	Ct
Elizabeth, N. J.	NY	..	Ct
Elmira, N. Y.	NY	M	Ct
El Paso, Tex.	NY	..	Ct
Elyria, Ohio	...	..	Ct
Erie, Pa.	NY	M	Ct
Evanston, Ill.	...	..	Ct
Evansville, Ind.	NY	M	Ct
Everett, Mass.	NY	M	Ct
Fairmont, W. Va.	...	..	Ct
Fall River, Mass.	NY	M	Ct
Fitchburg, Mass.	NY	M	Ct
Flint, Mich.	NY	M	Ct
Florida	NY	..	Ct
Fond-du-lac, Wis.	...	..	Ct
Fort Wayne, Ind.	NY	M	Ct
Fort Worth, Tex.	NY	..	Ct
Fresno, Cal.	...	..	Ct
Galesburg, Ill.	...	..	Ct
Georgia	NY	..	..
Gloucester, Mass.	NY	M	Ct
Grand Rapids, Mich.	NY	M	Ct
Green Bay, Wis.	...	M	Ct
Greenwich, Conn.	NY	M	Ct
Hagerstown, Md.	...	..	Ct
Hamilton, Ohio	...	M	Ct
Hammond, Ind.	...	..	Ct
Harrisburg, Pa.	NY	M	Ct
Hartford, Conn.	NY	M	Ct
Haverhill, Mass.	NY	M	Ct
Hawaii	NY	..	..
Hazleton, Pa.	NY	M	Ct
Holyoke, Mass.	NY	M	Ct
Huntington, W. Va.	NY	..	Ct
Hutchinson, Kan.	...	..	Ct
Idaho	NY	..	Ct
Illinois	NY	M	..
Indiana	NY	M	Ct
Indianapolis, Ind.	NY	M	Ct
Iowa	NY	M	..
Irvington, N. J.	NY	..	..
Jackson, Mich.	NY	M	Ct
Jacksonville, Fla.	NY	..	..
Jamestown, N. Y.	NY	..	Ct
Jersey City, N. J.	NY	M	Ct
Johnstown, Pa.	NY	M	Ct
Joliet, Ill.	...	..	Ct
Joplin, Mo.	...	..	Ct
Kalamazoo, Mich	NY	M	Ct
Kansas	NY	..	Ct
Kansas City, Kan.	...	..	Ct
Kansas City, Mo.	NY	M	Ct
Kearny, N. J.	NY	..	..
Kenosha, Wis.	...	..	Ct
Kentucky	NY	..	Ct
Kingston, N. Y.	NY	..	Ct
La Crosse, Wis.	...	M	Ct
Lafayette, Ind.	...	..	Ct
Lakewood, Ohio	...	M	..
Lancaster, Pa.	NY	M	Ct
Lansing, Mich.	NY	M	Ct
Lawrence, Mass.	NY	M	Ct
Lebanon, Pa.	...	..	Ct
Lewiston, Maine.	...	M	Ct
Lexington, Ky.	...	..	Ct
Lima, Ohio	...	M	Ct
Lincoln, Neb.	NY	..	Ct
Lockport, N. Y.	NY	..	Ct
Logansport, Ind.	...	..	Ct
Long Beach, Cal.	...	..	Ct
Lorain, Ohio	...	M	Ct
Los Angeles, Cal.	NY	M	Ct

State and City Bonds Legal for Savings Banks in New York, Massachusetts, and Connecticut—Continued

Bonds of	Legal in			Bonds of	Legal in			Bonds of	Legal in		
Louisiana	NY	..	..	Nashua, N. H.	...	M	Ct	Ohio	NY	M	..
Louisville, Ky.	NY	M	Ct	Nebraska	NY	M	..	Oklahoma	NY	..	..
Lowell, Mass.	NY	M	Ct	Nevada	NY	..	Ct	Olean, N. Y. ..	NY	..	Ct
Lynn, Mass.	NY	M	Ct	New Albany, Ind.	...	..	Ct	Omaha, Neb.	NY	M	Ct
McKeesport, Pa.	NY	M	Ct	Newark, N. J.	NY	M	..	Orange, N. J.	NY	..	..
Madison, Wis.	...	M	Ct	Newark, Ohio	...	..	Ct	Oregon	NY	M	Ct
Maine	NY	M	Ct	New Bedford, Mass.	NY	M	Ct	Oil City, Pa.	NY	..	Ct
Malden, Mass.	NY	M	Ct	New Britain, Conn.	NY	M	Ct	Oshkosh, Wis.	...	M	Ct
Manchester, N. H.	NY	M	Ct	New Brunswick, N. J.	...	..	Ct	Oswego, N. Y.	NY	..	Ct
Mansfield, Ohio	...	..	Ct	Newburgh, N. Y.	NY	..	Ct	Ottumwa, Iowa	...	..	Ct
Marion, Ind.	...	..	Ct	New Castle, Pa.	NY	M	Ct	Paducah, Ky.	...	..	Ct
Marion, Ohio	...	..	Ct	New Hampshire	NY	M	Ct	Parkersburg, W. Va.	...	..	Ct
Maryland	NY	..	Ct	New Haven, Conn.	NY	M	Ct	Pasadena, Cal.	NY	..	Ct
Massachusetts	NY	M	Ct	New Jersey	NY	M	..	Passaic, N. J.	NY	..	Ct
Medford, Mass.	...	M	Ct	New London, Conn.	NY	M	Ct	Paterson, N. J.	NY	..	Ct
Meriden, Conn.	NY	M	Ct	New Mexico	NY	..	..	Pawtucket, R. I.	NY	M	..
Middletown, Ohio	...	..	Ct	New York	NY	M	Ct	Pennsylvania	NY	M	Ct
Michigan	NY	M	Ct	Newport, Ky.	...	..	Ct	Peoria, Ill.	...	M	Ct
Middletown, Conn.	NY	M	Ct	Newport, R. I.	NY	M	Ct	Perth Amboy, N. J.	NY	..	..
Milwaukee, Wis.	NY	M	Ct	Newton, Mass.	NY	M	Ct	Philadelphia, Pa.	NY	M	Ct
Minneapolis, Minn.	NY	..	Ct	Niagara Falls, N. Y.	NY	M	..	Pittsburgh, Pa.	NY	M	Ct
Minnesota	NY	M	Ct	Norristown, Pa.	...	M	..	Pittsfield, Mass	NY	M	Ct
Mississippi	NY	..	..	Northampton, Mass.	NY	M	Ct	Plainfield, N. J.	NY	..	Ct
Missouri	NY	M	Ct	North Adams, Mass.	NY	M	Ct	Pontiac, Mich.	...	..	Ct
Moline, Ill.	...	..	Ct	North Carolina	NY	..	..	Portland, Maine.	NY	M	Ct
Montana	NY	..	Ct	North Dakota	NY	..	Ct	Portsmouth, Ohio	...	..	Ct
Montclair, N. J.	NY	..	..	Norwalk, Conn.	NY	..	Ct	Port Huron, Mich.	...	..	Ct
Muncie, Ind.	...	..	Ct	Norwich, Conn.	NY	M	Ct	Pottsville, Pa.	NY	..	Ct
Muskegon, Mich.	...	..	Ct	Oakland, Cal.	NY	M	Ct	Poughkeepsie, N. Y.	NY	..	Ct

Bonds of	Legal in		
Providence, R. I.	NY	M	Ct
Quincy, Ill.	...	..	Ct
Quincy, Mass.	NY	M	Ct
Racine, Wis.	NY	..	Ct
Reading, Pa.	NY	M	Ct
Revere, Mass.	NY	M	..
Rhode Island	NY	M	Ct
Richmond, Ind.	...	..	Ct
Rochester, N. Y.	NY	M	Ct
Rockford, Ill.	NY	M	Ct
Rock Island, Ill.	...	..	Ct
Rome, N. Y.	NY	..	Ct
St. Joseph, Mo.	...	..	Ct
St. Louis, Mo.	NY	M	Ct
St. Paul, Minn.	NY	M	Ct
Sacramento, Cal.	...	..	Ct
Saginaw, Mich.	NY	M	Ct
Salem, Mass.	NY	M	Ct
San Antonio, Tex.	NY	..	Ct
San Diego, Cal.	NY	..	Ct
Sandusky, Ohio	...	..	Ct
San Francisco, Cal.	NY	M	Ct
Scranton, Pa.	NY	M	Ct
Seattle, Wash.	...	M	..
Sheboygan, Wis.	...	M	Ct
Shenandoah, Pa.	...	..	Ct
Sioux City, Ia.	NY	M	Ct
Sioux Falls, S. D.	...	..	Ct
Somerville, Mass	NY	M	Ct
South Bend, Ind.	NY	M	Ct
South Carolina	NY	..	..
South Dakota	NY	..	Ct
South Omaha, Neb.	...	..	Ct
Spokane, Wash.	NY	M	Ct
Springfield, Ill.	NY	M	Ct
Springfield, Mass.	NY	M	Ct
Springfield, Mo.	...	M	Ct
Springfield, Ohio	NY	M	Ct
Stamford, Conn.	NY	M	Ct
Steubenville, Ohio	...	..	Ct
Stockton, Cal.	...	..	Ct
Superior, Wis.	...	M	Ct
Syracuse, N. Y.	NY	M	Ct
Tacoma, Wash.	NY	..	..
Taunton, Mass.	NY	M	Ct
Tennessee	NY	..	Ct
Terre Haute, Ind.	NY	..	Ct
Texas	NY	..	Ct
Toledo, Ohio	NY	M	Ct
Topeka, Kan.	...	..	Ct
Torrington, Conn.	NY	M	Ct
Trenton, N. J.	NY	M	Ct
Troy, N. Y.	NY	M	Ct
Utah	NY	..	..
Utica, N. Y.	NY	..	Ct
Vermont	NY	M	Ct
Waco, Tex.	...	..	Ct
Waltham, Mass.	NY	M	Ct
Washington	NY	M	Ct
Waterbury, Conn.	NY	M	Ct
Waterloo, Ia.	...	..	Ct
Watertown, Mass.	NY	M	..
Watertown, N. Y.	NY	..	Ct
West Virginia.	NY	..	Ct
Wheeling, W. Va.	NY	..	Ct
Wichita, Kan.	NY	..	Ct
Wilkes-Barre, Pa.	NY	M	Ct
Williamsport, Pa.	NY	M	Ct
Wilmington, Del.	NY	M	..
Wisconsin	NY	M	Ct
Woonsocket, R. I.	...	M*	..
Worcester, Mass.	NY	M	Ct
Wyoming	NY	..	Ct
York, Pa.	NY	M	Ct
Youngstown, Ohio.	NY	M	Ct
Zanesville, Ohio	...	..	Ct

EXPLANATORY: This compilation embraces only State bonds and bonds of cities having a population according to the 1920 Census of 20,000 or more. The savings bank law of Connecticut requires cities in States outside of Connecticut to have a population of at least 20,000. Therefore, this list is complete as to Connecticut. The New York savings bank law requires a population of not less than 45,000, but a recent amendment waives the population requirement so far as municipalities in States adjacent to New York are

State and City Bonds Legal for Savings Banks in New York, Massachusetts, and Connecticut—Continued

concerned. The Massachusetts population requirement is 100,000 for cities in some States, 30,000 for cities in other States, and for cities, counties or towns in Maine, New Hampshire, Rhode Island and Connecticut only 5,000 population is required. If all the small communities in these States where a very small or no minimum population is required could be listed, this tabulation would be so long as to be impracticable. Furthermore, it would probably be impossible to present at any one time a complete and accurate list embracing all of these smaller communities.

Since all New York municipals are legal in New York, all Massachusetts municipals are legal in Massachusetts, and all Connecticut municipals are legal in Connecticut, this list includes only those cities, located in the three States mentioned, whose bonds are legal in one or both of the two States other than its own.

* Only bonds issued prior to June 8, 1908, are legal.

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Hoffman & Wood: "Taxation of Federal, State and Municipal Bonds." Privately printed in 1921.

Also see a very valuable "Digest of Opinions of Attorney General of New York State Relative to Legality of Municipal Bonds as Investments for Savings Banks and Trustees." Prepared for E. H. Rollins & Son, by Messrs. Hoffman and Wood, 1922.

Chapter XIII

TAXATION OF BONDS

Complexity of our tax assessments.—The complexity of our tax assessments and the conflict of tax influence caused by the defaults, laws and rates of the several States, and their political subdivisions, and the over-shadowing influence of the present system of Federal taxation made necessary by the late war, prevent an exhaustive treatment of the subject in a book of this character. Only an outline of general principles can be given here. In the application of general principles, simplicity is desirable. For this reason, we shall consider the theoretical effect of a tax upon the ordinary corporation bond.

Direct personal property tax versus income tax.—The two generally recognized taxes in the United States affecting such a bond are direct personal property taxes and income taxes. The personal property tax is generally imposed upon the principal of the bond. The income tax is imposed upon the interest the bond bears. To realize the effect of a personal property tax upon the principal of the bond, take the hypothetical case of a bond owned in a State having no personal property tax and no income tax. If such a State were to pass a law imposing a one per cent tax upon the principal of a $1,000 bond bearing five per cent interest, the owner would be obliged to pay $10 in taxes each year. This would reduce the income on the bond from $50 to $40 a year. If the State, instead of enacting the personal property tax just stated, were to pass an income tax law taxing the interest of the bond at the rate of twenty per cent, the owner would be obliged to pay $10 in taxes each year. This would make exactly the same reduction in his income from the bond, which would then yield only $40 a year. It may be seen, therefore, because as a general proposition all taxes are paid out of income, that it is immaterial, in considering the effect of a tax on the bond, whether the tax is based upon its prin-

cipal or income. If the owner of the bond has a capital of $100,000 consisting entirely of similar bonds, the effect of the tax in either case is a reduction of his income from $5,000 to $4,000 a year so long as he holds the bonds and they are subjected to such taxes.[1]

The effect of the taxation of the income from bonds is shown in the table entitled "Tax Free v. Taxable Bonds," following this chapter. It will be observed that in the case of an individual whose income, subject to surtaxes, is between $10,000 and $12,000, he must receive 4.44 per cent net income, to be as well off as he would be with a municipal bond from which he receives a non-taxable income of 4 per cent per annum. As the amount of surtaxes increases, the discrepancy is more marked. The fortunate individual whose income exceeds $200,000 a year, must receive 9.53% to obtain as much income as he would obtain from a 4 per cent municipal bond.

Definition of the taxing power.[2]—The power to tax is essentially incident to sovereignty. It arises out of necessity and is possessed by all sovereign States. Necessarily, it is limited to subjects within the jurisdiction of the State. Those subjects are persons, property, and business. Whatever form taxation may assume, it must relate to one of these subjects.

Taxing power of the United States.—Power "to lay and collect taxes, duties, imposts and excises" is conferred upon Congress by Art. 1, Sec. 8 of the Constitution of the United States. That this power is exhaustive and embraces every conceivable power of taxation, has never been questioned, but it is also conceded that it is subject to the limits, expressed or implied, contained in other sections of the Federal Constitution.

Limitations upon the Federal taxing power.—The Constitution of the United States contains three express limitations upon the power of taxation conferred upon the Federal Government. All duties, imposts and excises are required to operate uniformly throughout the United States. Taxes or duties on articles exported from any State are prohibited, and capitation and other direct taxes, except income taxes, are

[1] Annals, p. 156.

[2] Much of the following material is derived from "Taxation of Federal, State and Municipal Bonds" by Messrs. Hoffman and Wood, to which the student is referred for a more complete treatment of the subject.

also prohibited, unless levied in proportion to the census or enumeration directed by the Constitution to be taken. Many limits upon this power are also implied from the nature of our federal form of government and from other express limits imposed upon the Federal Government by the Constitution.

Taxing power of the States.—The States composing the United States are sovereign States, and the power of taxation is, therefore, inherent in each State.

Unless restrained by the provisions of the State or Federal Constitution, the power of a State as to the mode, form and extent of taxation is unlimited, where the subjects to which it applies are within its jurisdiction. The legislature levying the tax is the sole and ultimate judge of the expediency or necessity of requiring it and of the extent to which it shall be charged upon any class of taxable subjects. Hence, in the absence of constitutional limitation, the legislature may select the subjects of taxation and upon those subjects only, may the taxing officials of the State extend the tax. Subjects not selected for taxation by the legislature are commonly designated as "exempt from taxation."

Limitations upon the taxing power of the States.—Many limitations are imposed upon the taxing power of the States by the Constitution of the United States. By the fourteenth amendment, the States are prohibited from depriving citizens of property without due process of law, and this amendment has been construed as prohibiting the levy of taxes except for public purposes. It is also well settled that a State cannot tax bonds of the United States or its Territories without the consent of the Congress.

Purposes for which taxes may be levied.—The power of taxation, moreover, can be exercised only for public purposes. In the leading case upon this subject, Mr. Justice Miller said, "To lay with one hand the power of the government on the property of the citizen, and with the other bestow it upon favoured individuals to aid private enterprise and build up private fortunes, is none the less a robbery because it is done under the forms of law and is called taxation. This is not legislation. It is a decree under legislative forms. Nor is it taxation." [3]

[3] *Loan Association v. Topeka* (1874), 20 Wall (U. S.) 655 at 664.

Taxation of the principal of State and municipal bonds by the United States.—As the power to tax is the power to destroy, to admit the power of the Federal Government to tax the States, or their instrumentalities of government, would completely subordinate the States to the Federal Government. It is, therefore, well established that it is not within the power of the United States to tax a State or its governmental instrumentalities, and, as to tax a bond issued by a State or one of its subdivisions is to tax a governmental function, it is well established that the power to tax such obligations is not vested in the United States.

Taxation of the principal of State and municipal bonds by the States.—While a State may exempt State or municipal bonds from taxation, unless prohibited by its constitution from doing so, it may refuse to grant such an exemption. It is well settled that, in the absence of constitutional limitations, the power of taxation extends to and embraces the bonds of the State and its municipalities.

In levying a tax upon such bonds, however, the State may not impair the obligation of the contract with the holders of the bonds and the coupons representing the interest thereon.

The bonds of other States or of the municipalities of other States may be taxed if located within the limits of the State levying the tax, or owned by residents of that State. Statutes levying such taxes do not violate the Federal Constitution, as the several States, in ratifying that instrument, did not enter into a covenant preventing one State from taxing the public securities issued by another State, her counties, or municipalities. The State may also authorize its political subdivisions to tax public securities, including the bonds of the subdivision levying the tax, but only when the security itself or its owner is within the jurisdiction of the State.

Taxation of the income from State and municipal bonds: nature of the tax.—The Federal Government and many of the States have enacted statutes taxing income. While many of these statutes were passed pursuant to express constitutional provisions authorizing the enactment of such laws, the power of the legislature to tax incomes does not depend upon a constitutional grant. The power of taxation is plenary and includes all methods of taxation.

Such taxes are not property taxes within the meaning of constitutional provisions requiring taxation of property to be

equal and uniform, and accordingly, graduated taxes have been uniformly sustained as constitutional. Nor are such taxes to be considered as direct personal taxes or privilege taxes.

Non-residents, therefore, may be subjected to such taxation based upon the income earned in the State or received from residents of the State without violating the Federal Constitution, and a State may tax income derived from bonds owned by a non-resident, if the bonds are located in the State, but not otherwise. Not being personal taxes, the State levying the tax need not have jurisdiction over the person entitled to the income taxed. The fact that the property from which the income is derived is also taxed, does not render a tax upon such income void for double taxation, the income being regarded as a distinct subject of taxation. In most States there is no legal obstacle to double taxation.

Taxation of income of State and municipal bonds by the United States.—As the Constitution read prior to the adoption of the sixteenth amendment, the Federal Government had no power to levy income taxes unless apportioned between the States. This was decided in the Pollock case.[4] Thereafter the sixteenth amendment to the Constitution was adopted and became effective February 25, 1913. This provides as follows: "The Congress shall have power to lay and collect taxes on incomes from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration."

Effect of the sixteenth amendment to the Federal Constitution.—Since the adoption of this amendment, the question has arisen whether the taxing power of the United States has been extended, through its adoption, so as to permit of the taxation by the Congress of the income derived from bonds of the various States, and of the subdivisions thereof. Some diversity of opinion appears to exist among eminent authorities, and so far the question has not been directly passed upon by the United States Supreme Court. It is the general opinion that no additional powers of taxation have been devolved upon the Congress by virtue of the sixteenth amendment, or to state it differently, that property or the income from property which could not be taxed prior to the adoption of the sixteenth amendment, cannot now be taxed unless the tax

[4] *Pollock v. The Farmers' Loan and Trust Co.* (1895), 157 U. S. 429.

is apportioned between the States. The writer, however, strongly dissents from this view. The words "from whatever source derived" must be construed in accordance with the ordinary rules of statutory construction; they must be given effect irrespective of the thoughts in the minds of the originators of the phrase, or in the minds of the advocates or opponents of the amendment. If the words are to be given their ordinary meaning in the English language, it would seem there can be no doubt that additional power to tax has been granted to the Congress. It is contended, therefore, that although the Congress has not as yet attempted to tax the interest on municipal bonds, it has the power to levy such a tax under the provisions of the sixteenth constitutional amendment.

Taxation of income of State and municipal bonds by the States.—Income from State and municipal bonds is taxable by the State of issue when such bonds are owned by its citizens. Can the State, however, levy such a tax upon the income derived from a bond which it has contracted to exempt from taxation? The right of the State to tax the income of such bonds does not appear ever to have been decided. On principle, however, it would seem that it is not within the power of a State to tax such income. It is well established that a tax upon the income of a bond is a tax upon the security. It is for this reason that a State cannot tax the interest of bonds of the Federal Government. It would seem to be no less a tax upon the security when it is levied by a State upon the income of a State or municipal bond. If the bond is exempt from taxation by a contract, protected by the Federal Constitution, in what respect does the taxation of the income derived from such a bond differ from the taxation of the income of bonds of the United States?

When a bond is issued under such circumstances that a contract for an exemption from taxation arises, or when for a valuable consideration the State has contracted to exempt a bond from future taxation, the State may not violate such contract by taxing the bond under the guise of taxing the income derived therefrom.

When, however, the exemption from taxation is not a contract right, it may be withdrawn at any time by the State. Under such circumstances, there seems to be no reason why the State may not tax the income of the bond. If it might

withdraw entirely the exemption, it clearly can withdraw it to the extent of subjecting to taxation the income derived from the bond.

Taxation of bonds of non-residents.—As to the taxation of public securities belonging to non-residents, it is well settled that such securities are in such concrete, tangible form that they are subject to taxation where found irrespective of the domicile of the owner and a State may declare that, if found within its limits, they shall be subject to taxation. The statutes of most States accordingly provide for the taxation of such securities in the hands of non-residents either expressly or by providing that all personal property within the State shall be subject to taxation.

Situs for taxation.—The physical presence of the bond within the limits of the State is essential to give the State jurisdiction to tax it, when owned by a non-resident. The power of taxation is confined to the territorial limits of the State and it is not within the power of a State to tax bonds owned by a non-resident unless it has acquired jurisdiction over the bonds by reason of their presence in the State. An attempt to tax property not within the jurisdiction of the State violates the Constitution of the United States by depriving the owner thereof of property without due process of law.

Mere temporary presence of property within the limits of the State is not sufficient to confer jurisdiction. Therefore, a bond sent into a State for collection, registration, sale or exchange, etc., by a non-resident, is not subject to taxation by that State.

Inheritance taxes.—An inheritance, succession, or decedent's estate tax, so called, is a tax on the succession and not on the property itself. The right to take property by devise or descent is the creature of the law and the authority which confers the right may impose conditions upon it.

The States and the United States may tax the privilege, discriminate between relatives and between these and strangers, and grant exemptions. As the tax is not levied upon the property which passes to the heir or devisee, *but upon the right to take the property by will or descent,* the character of the property passing is immaterial. Hence, limitations upon the right of the Federal Government to tax the instrumentalities of the States, or *vice versa,* do not apply to inheri-

tance taxes. The State or Federal Government may lawfully measure the amount of tax by referring to the value of the property passing. The incidental fact that such property is composed, in whole or in part, of Federal or municipal bonds does not affect the validity of the tax.

In considering taxation and its effect, it must be remembered that the purpose of taxation is to raise money for the necessities of government, whether national, federal or municipal. Taxing acts are not always fair or equitable, and they are not necessarily intended to be. Government cannot exist without the means to carry it on, and the following quotation from Bernard Shaw's *Cæsar and Cleopatra,* illustrates the point:

Rufio (bluntly). You must pay, Pothinus. Why words? You are getting off cheaply enough.

Pothinus (bitterly). Is it possible that Cæsar, the conqueror of the world, has time to occupy himself with such a trifle as our taxes?

Cæsar. My friend: taxes are the chief business of a conqueror of the world.

Tax-Free vs. Taxable Bonds

A Chart Showing the Effect of Federal Income Tax on Yield from Tax-Free and Taxable Bonds in 1922

Income from certain U. S. Government, State and municipal bonds is exempt from the Federal income tax, rate of which, for 1922 income, ranges from 4% to 58%, according to amount of income. This table has been compiled to indicate the approximate yield which taxable bonds must return to equal the return from tax-free bonds yielding from 4% to 6%.

Example: Individual with income (subject to surtaxes) of about $50,000 purchases taxable bonds yielding 6.52%, the income from which is subject, in his hands, to a normal tax of 8% and a surtax (on income between $50,000 and $52,000) of 23%, or a total of 31%. Deducting the tax, his income from this bond is reduced to 4.50%. In other words, for this person a tax-free bond yielding 4.50% would be equivalent to a taxable bond yielding 6.52%. In the table below, the top line or row of figures represents yield (or basis) from tax-free bonds. In columns below is shown equivalent yield from taxable bonds when income (total amount subject to surtaxes) corresponds to amounts shown in extreme left-hand column.

This table is offered as a guide to assist the purchaser of bonds to choose intelligently between taxable and tax-free investments. It is computed on the theory that any change in an individual's taxable income resulting from a switching of investments from a taxable to a tax-free status, or vice-versa, is effective at the highest brackets or the "top" of his income and, hence, the highest surtax rate has been applied in computing these equivalent yields. Because of the change of tax rates from year to year, it is useless to attempt an exact computation of the value of tax exemption over a series of years and for this reason we believe the chart is sufficiently comprehensive to serve the purpose for which it is intended.

Income (Subject to Surtaxes) Between	4%	4¼%	4⅜%	4½%	4⅝%	4¾%	4⅞%	5%	5⅛%	5¼%	5½%	5¾%	6%
$10,000 & 12,000	4.44	4.72	4.86	5.00	5.14	5.28	5.42	5.56	5.69	5.83	6.11	6.39	6.67
20,000 & 22,000	4.76	5.06	5.21	5.36	5.50	5.65	5.80	5.95	6.10	6.25	6.55	6.85	7.14
24,000 & 26,000	4.88	5.18	5.34	5.49	5.64	5.79	5.95	6.10	6.25	6.40	6.70	7.00	7.31
28,000 & 30,000	5.00	5.31	5.46	5.62	5.77	5.93	6.09	6.25	6.41	6.56	6.87	7.18	7.50
32,000 & 36,000	5.19	5.51	5.67	5.84	6.00	6.16	6.32	6.49	6.66	6.81	7.14	7.46	7.79
40,000 & 42,000	5.40	5.73	5.90	6.07	6.24	6.41	6.58	6.75	6.93	7.09	7.43	7.77	8.11
44,000 & 46,000	5.55	5.90	6.07	6.25	6.42	6.59	6.77	6.94	7.12	7.29	7.63	7.98	8.33
50,000 & 52,000	5.80	6.16	6.34	6.52	6.70	6.88	7.06	7.25	7.43	7.61	7.97	8.33	8.69
54,000 & 56,000	5.97	6.34	6.52	6.71	6.89	7.08	7.27	7.46	7.65	7.84	8.21	8.58	8.96
60,000 & 62,000	6.25	6.64	6.83	7.03	7.22	7.42	7.61	7.81	8.00	8.18	8.58	8.96	9.37
64,000 & 66,000	6.45	6.85	7.05	7.26	7.46	7.66	7.86	8.06	8.27	8.46	8.86	9.27	9.68
70,000 & 72,000	6.78	7.20	7.41	7.62	7.81	8.04	8.25	8.47	8.69	8.90	9.33	9.75	10.17
74,000 & 76,000	7.01	7.45	7.67	7.89	8.11	8.33	8.55	8.77	8.99	9.21	9.65	10.07	10.53
80,000 & 82,000	7.40	7.86	8.09	8.33	8.56	8.79	9.02	9.25	9.49	9.71	10.18	10.64	11.10
84,000 & 86,000	7.68	8.16	8.40	8.65	8.89	9.13	9.37	9.62	9.86	10.09	10.57	11.04	11.52
90,000 & 92,000	8.16	8.68	8.94	9.20	9.45	9.70	9.95	10.20	10.46	10.71	11.21	11.73	12.25
94,000 & 96,000	8.51	9.04	9.31	9.58	9.84	10.10	10.36	10.62	10.90	11.16	11.70	12.23	12.77
100,000 & 150,000	9.10	9.66	9.94	10.22	10.50	10.79	11.07	11.36	11.65	11.93	12.50	13.07	13.65
150,000 & 200,000	9.31	9.89	10.18	10.47	10.76	11.05	11.34	11.63	11.92	12.21	12.80	13.38	13.95
Over 200,000	9.53	10.12	10.42	10.72	11.02	11.32	11.62	11.92	12.20	12.51	13.10	13.69	14.29

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Chapter XIV

VALUATION OF BONDS

There is no golden rule for the valuation or appraisal of bonds, whether municipal or other. The much overworked word "relativity" may be used in describing the mental and mathematical processes involved in determining purchasing and selling price, but the word should be "paid extra." As Humpty Dumpty says to Alice in "Through the Looking-Glass": "When I make a word do a lot of work like that, I always pay it extra."

Money a commodity.—Money is a commodity, and its price, or the price of its use, fluctuates in tides and is, except when prices are "pegged" during a national emergency, governed by the laws of supply and demand. The buyer of a bond holds a written promise to pay a specified sum of money to the owner of the bond on a specified date. The maker of the bond, whether individual or corporate, promises to pay interest for the use of the money. In ordinary terms, the bondholder makes a loan and is paid for making it. How much he is paid is governed by many factors, summed up in the words "market conditions" existing at the time the loan is made.

Interest.—Interest is the amount paid, at annual, semi-annual, or quarterly periods for the use of money. It is measured by a percentage of the sum borrowed and in modern times such percentage has been from two to eight per cent or more. Gorgeous rates of interest, such as ten per cent a month or one hundred and twenty per cent a year, have passed with the happy frontier days of the Golden West when property was as insecure as life.

Nominal yield.—Disregarding theories of present value, and compounding interest return, the sum of money actually paid for the use of $1,000 at five per cent for twenty years is $1,000, which is the nominal yield, and the net yield, if the bond is purchased at par.

Net yield.—Bonds are rarely purchased or sold at par, but "at a premium" which is above par, or "at a discount" which is below par. Now it is evident that a bond purchased at a discount gradually appreciates in value as it approaches maturity, and a bond purchased at a premium depreciates for the same reason. The amount received as interest is not the true income if the principal either appreciates or depreciates. In such cases, the real income is determined by the actual income, reduced by the amount of depreciation of principal, or increased by the amount of appreciation. For a further discussion of both depreciation and appreciation, the reader will do well to consult "Jordan on Investments." [1]

Tables of bond values.—These are used to determine net yield, when price, face value, and date of maturity are known, and to ascertain the price at which a bond of known face value and maturity must be purchased to yield a certain desired return. The mathematical and accounting theories upon which the soundness of such tables depends are highly interesting, but neither a statement nor a discussion of such theories has any place here. The student is referred to Jordan,[2] Rollins,[3] Chamberlain,[4] and other writers. The point for the reader to observe is that by the use of such tables, we can determine the basis or net yield upon which bonds sell, and the basis, so determined, measures the value of the investment. If the basis or net yield is 5.40, the investor has a cheaper bond than he has if the basis is 3.10. The expression "net income basis" is frequently used for and is more accurate than either "basis" or "net yield."

Fluctuations in the net income basis are shown in the chart following this chapter. By reference to it, the rise and fall of prices since 1900 may be studied, and it will be observed that bonds were highest in 1901, the basis being 3.10 and lowest in September, 1920, the basis being 5.25. The sudden and unexpected rise is noteworthy, beginning in July, 1921, and temporarily suspended in December, 1921.

The prices obtained twenty years ago by an investment banking house are shown in the copy of an advertisement of Messrs. Harris Forbes & Company, taken from the New

[1] Jordan, p. 276.
[2] p. 274.
[3] Annals, p. 12.
[4] pp. 405 and 426.

York *Sun* of November 1, 1921, following this chapter. The "net returns" may be compared with the "yield per cent" of various issues during the weeks ending December 16 and December 30, 1921, shown in the tables taken from the New York *Times* of December 17 and December 31, 1921.

The income basis on which New York City bonds have sold from 1907 to 1921 is shown in the schedule "Results of New York City Bond Sales" abbreviated from a table published in the *Bond Buyer* on December 16, 1921, following this chapter.

Differences in yield between different maturities of the same issue of bonds, sold at a discount, at par and at a premium, are shown in the advertisement of $31,800,000 State of New York 5s, offered June 10, 1921, a copy of which follows this chapter. The earlier maturities offered at a discount yield more than the coupon rate of interest. The bonds maturing in the year 1931 and thereafter, offered at increasing premiums as the term lengthens, yield less than the coupon rate of interest or slightly more than 4.70.

Purchasing power of the dollar.—It must not be overlooked that the purchasing power of money varies from time to time, and tends to increase or to decrease over long periods. The rise in the cost of living during the World War and thereafter is fresh in our recollection. The gradual, too gradual, decline is hailed with delight. If it cost $5,000 a year to live in 1910 and costs $10,000 a year in the year of Grace 1922, the yield of interest at six per cent purchases only what the yield at three per cent would buy a decade ago. A chart showing wholesale prices in the United States for 110 years, reproduced with the permission of Col. Leonard P. Ayers (Vice president of The Cleveland Trust Company), from "Price Changes and Business Prospects" follows this chapter. The price chart shows mountainous peaks during and after the War of 1812, the Civil War and the World War. In each case, prices rose to far more than twice the normal. After the first two wars, prices declined precipitously for about five years and then more slowly for 25 or 30 years. We may reasonably infer that prices will continue to decline for several years.

Market conditions.—Market conditons are a resultant of causes and events, some extending over a period of years, such as gradually rising commodity prices, and some immedi-

ate, such as panics. The general industrial condition of the country (calling or not calling for new money) depends upon numerous important factors. In substance, it is the demand for money which determines its price and this price is interest.

The value of a bond has been said to be the capitalized value, at the current interest rate paid for short-time money, of the amount of its yield. If the current interest rate rises very sharply, and the high rate is believed to be only temporary, the price of bonds will not be materially affected. Stated differently, it is said that the price of bonds varies inversely with the rate of interest paid for short-time money.[5]

Bonds are not equally valuable.—In the preceding chapter, the elements of a sound investment were discussed, and in other chapters differences were shown between the powers of municipalities or quasi-municipalities and between unqualified and qualified promises to pay. There must be a difference in value between a $1,000 water bond of New York City and the bond of an irrigation or drainage district, although they bear the same interest rate and have the same term. One is the unqualified promise of the country's largest city to pay at all events. The other is the promise to pay if the project is successful and taxes (or assessments) are collected. The first bond may sell for 105.75. The second may sell for 80.

Differences in value then exist between the bonds of one city and another, as well as between the bonds of a city and, for example, a school district. The purpose of issue may affect value very materially. In Chapter XVI, devoted to particular bonds, will be found statements of the peculiarities of bonds of different issuing subdivisions and of bonds issued for various purposes.

Differences in value as between municipalities.—As between municipalities, several factors must be taken into consideration; or, if the value of the bonds of A is to be estimated, by a consideration of the value of similar bonds of B. These factors are:

1. Assessed valuations of taxable real property.
2. Indebtedness.
3. Tax rates.
4. Population and
5. Credit.

[5] Annals, p. 202.

The factors being equal, the bonds of A, having an assessed valuation of ten million dollars, are better than the bonds of B which have an assessed valuation of five million dollars. Or again, other factors being equal, the bonds of A with a debt of five hundred thousand dollars are better than the bonds of B with a debt of seven hundred and fifty thousand dollars. If the tax rate of A is greater than that of B, the burden on the landowner is greater and the nearer is land in A to the tax saturation point. The ability of land to bear taxation is smaller than might be supposed by any but the well-informed. The larger population of B indicates growth, industry, and power to pay. And A, having an unbroken record of paying its debts, is in much better position to borrow (and its bonds will be more eagerly sought for) than B which has defaulted at some time in the past.

Assessed valuation.—"Assessed valuation, or assessment, an item always on the bond circular * * * is not hard to understand. It is the value put on property by assessors as the basis for taxation. The 'grand list' of certain States, e.g. Connecticut, is a synonym. * * * The 'tax duplicate' is another synonym." [6] So is the "abstract of ratables" in New Jersey. "Assessed valuation is of importance chiefly in its relation to the tax rate and to real valuation. Real valuation, in its turn, is liable to different interpretations from different assessors" [7] in different States and in different places in the same State.

In any comparison of assessed valuations, only real estate valuations should be considered and the ratio of real value to assessed value must be determined. In a certain New York town some years ago, the assessed valuations were twenty-five per cent of the real, despite the statute requiring assessment at the real value. Thus the town escaped paying its fair share of the State and county tax, efforts of the board of equalization to the contrary notwithstanding. As the borrowing power of this town was and is ten per cent of the assessed valuation, its ostensible borrowing power was only one-quarter of its real limit based on an honest assessment and the tax rate was of course very high.

Comparison of assessed valuations of the same city for a period of years is sometimes of value, but care must be

[6] Chamberlain, p. 191.
[7] *Id.*, p. 192.

exercised to make necessary allowance for changes in the basis of assessment. For example, the taxable values may have been sixty per cent in past years and the ratio of real to assessed values increased or decreased.

Indebtedness.—The indebtedness of a municipality is either gross or net. In considering indebtedness, it is well to state separately the bonded debt, floating debt, contract debt, and the water debt. This segregation is important because a "set up" in one way may not answer all questions.

Whether a bond is a legal investment for fiduciaries in New York State is determined somewhat differently from whether it is available to secure postal savings deposits. The requirements which bonds must possess to be available for investment by trustees and other fiduciaries, and to satisfy the regulations of the postal savings department, are referred to in Chapter XII. For example, a bond to be a legal investment for a trustee in New York must be that of a municipality of which the net debt does not exceed seven per cent of the taxable property, but to be acceptable for postal savings deposits, the municipality may have a net debt of ten per cent.

Net debt may mean bonded and floating debt, less sinking funds, cash on hand for redemption of bonds falling due in the current year, and, for certain purposes, less water debt or debt incurred for public utilities which in contemplation of law are self-sustaining. The economic net debt is the indebtedness to pay for which a tax must be levied. For illustration of debt statements, see Chapter VI, and the forms therein referred to. Comparison of indebtedness should obviously be made only when the indebtedness is set up in the same way.

Tax rates.—Tax rates are very difficult to compare. If A assesses the taxable property at 50% of its true valuation, and raises the same amount of money as B which assesses real property of the same true value at its true value, the tax rate of A will be twice that of B. Yet the bonds of A may be quite as good as those of B. For purposes of comparison, the assessed valuations of both municipalities must be equalized, and it is "desirable to separate the city tax from the county and States taxes." [8] And "there will often be distinct and special assessment taxes of one sort or another * * * not included even in the 'total tax,' but which are imposed, never-

[8] Chamberlain, p. 182.

theless, upon such a large portion of the property within the corporate limits that they cannot legitimately be overlooked." [9] A large western city which has a low tax rate assesses the cost of sewers, parks, alleys, and sometimes streets, upon property claimed to be specially benefited. The assessment areas have been known to take in practically the entire taxable property of the city. Inquiry should be made whether the municipality is at the same time a school or other tax district, and if so whether the school or other tax is included in the total rate given by officials.

The saturation point of taxation is relatively low. Three per cent on improved property assessed at its true value becomes noticeable; three and one-half per cent may be a burden; and a higher rate may absorb the owner's income from the property. Vacant property may be, and very frequently is, abandoned by the owner after the accumulation of a few years' taxes renders it costly to redeem. A second-class city in New York had over five million dollars unpaid taxes on its books within the past three years. Hence a high tax rate may be an indication of insecurity.

Population.—Population as a factor in valuation has little importance, beyond a certain point. A village having two hundred people will have a low assessed valuation and little debt; a city having half a million inhabitants will have substantial assessable values and sufficient excuse for existence for it to borrow money to pay for improvements. Growth of population is an indication of industrial and commercial growth which might not otherwise be revealed. Population may also suggest poll or capitation taxes. The more people, the larger the return from such taxes will be, but a poll tax is too uncertain and too small in amount to be a factor of security. Population must be known before availability for postal savings deposits can be determined.

Credit is the single most important factor.—A recent default, even carelessness in meeting interest payments, is a most serious matter from the dealers' or investors' standpoint. A great deal can be said about the meaning of municipal credit, and the fiscal history of counties and even States which have defaulted, but it can all be summed up by saying that a city's credit is shown by its financial history. Much water must run under the bridge before the consequences of

[9] Chamberlain, p. 182.

a default will cease to be reflected in the value of a city's bonds.

In practice, the valuation of bonds is described as follows by a buyer for a reliable and conservative investment house:

A Study of the Comparative Market Value of State and Municipal Bonds

State and municipal bonds may be divided into two classes:

1. Those that are direct obligations secured both by the full faith and credit of the State or political subdivisions, and in the case of the latter, supported by unlimited ad valorem taxes.

2. Those that are limited obligations of the State or political subdivision supported by special revenues or special taxes levied on properties benefited.

The question of rating, or the comparative market value of bonds in either of these classes, may best be studied by listing the various requirements generally sought for by investors.

Class 1

A. Financial statement and population.

1. Net debt within 5 per cent of assessed valuation is very conservative and with population of 30,000 or more, bonds have a very wide market.
2. Net debt within 7 per cent of assessed valuation is conservative, and with population of 100,000 or more, bonds have a wide market.
3. Net debt over 7 per cent of assessed valuation passes the dividing line between first-grade and second-grade bonds. This is not a hard and fast rule, as there are many cities with over 7 per cent net debt whose bonds are unquestionably sound, but the market for their bonds is not as general.

Bonds under subdivisions 1 and 2, when meeting all other requirements, are legal investment for savings bank and trust funds in New York and New England. With few exceptions, bonds in Class 3 are not legal.

4. Character of population of small communities, such as villages, towns, school districts and sparsely settled counties, is of the utmost importance and must always be considered.

B. Denomination—Coupon—Registration.

1. Denominations of $1,000 have the best market; $500 bonds are acceptable; smaller denominations are not desirable.
2. Coupon bonds which may be registered as to principal or registered as to both principal and interest are preferable. If interchangeable from fully registered to coupon, so much more desirable; however, but few cities provide for this.
3. Fully registered bonds have only a limited market.

C. Place of Payment of Principal and Interest.

If market for bonds is sought in the East, payment of principal and interest should be in New York. Local payment of principal and interest detracts from the market value, and since the demand for bonds payable in gold is very limited, where this is provided, it does not add materially to the value of the bond.

D. Purpose of Issue and Maturity.

Briefly, it is desirable that the life of the bond be within the life of the improvement. Bonds issued for improvement of a permanent character are preferred. The economic soundness of the purpose of the issue is given careful consideration by thoughtful investors.

E. Local Tax Exemption.

In certain States all current issues of bonds are exempt from State and local taxation. Where bonds are exempt from State and local taxation, they generally sell at a lower return (or higher price) than taxable bonds. It is accordingly necessary to know to what extent bonds are exempt from such taxation.

F. Legal Features.

1. Marketable legal opinion.
2. Limited or unlimited taxes.
3. Voted or unvoted bonds. (A "voted" bond evidences popular assent.—*Author.*)
4. Debt limit.
5. Provisions for retiring bonds at maturity.

G. Premiums and Discounts.

Premium bonds are not generally desired by individual investors but most of our large institutions and estates now amortize premiums. The market for a bond with a high premium is not quite as good as the market for a discount bond.

H. Summary and Conclusion.

If we find a new issue of bonds has all the features desired, we ascertain in what States it is a legal investment for trust funds and savings banks. From this we estimate the extent of the market for possible demand for the bonds.

The next question is whether the bonds will have to be marketed at a premium, and if so, to what extent this premium will adversely affect the sale.

Finally, the maturity of the issue is considered. If the bonds mature all at one time, the conclusion as to what is the market value is promptly arrived at, but where the issue matures serially, each maturity must be considered separately.

The question of market value is decided by the old law of supply and demand and money market conditions. It is possible to put in writing only comparative values of municipals, and the above is an attempt to cover the subject briefly. Much more may be said. Each of the above subdivisions is a study in itself.

Class 2

Most of the requirements covering bonds in Class 1 might be applied to those in Class 2. We may emphasize, however, that the purpose of the issue, the character of the community borrowing the money and the legal features must be more carefully investigated in determining the value of bonds in Class 2, as against direct obligation bonds issued by States and their political subdivisions.

R. M. S.

Differences of opinion in evaluating bonds.—That differences of opinion exist even between highly competent experts is shown by a consideration of the bids submitted for issues of Binghamton, New York, Bonds:[10]

BINGHAMTON, N. Y., Oct., 1921.

Messrs. Blodget & Co. of New York were the successful bidders for the following bonds aggregating $116,200, paying a premium of $4,089.08—103.519, a basis of 4.96%:

Park Creek Imp. 10 1/4 year (average)	$ 40,000
Pierce Creek Imp. 9 1/4 year (average)	36,000
Oak St. School 9 1/4 year (average)	18,000
Broad Ave. School 8 1/4 year (average)	16,700
Cross St. Bridge 6 3/4 year (average)	6,500

Other bidders were:

Barr & Schmeltzer	103.678
Sherwood & Merrifield	102.64
George B. Gibbons & Co.	102.52
C. H. White	102.186
Ogilby & Austin	101.96
Peoples Trust Co., Binghamton	101.749
National City Co.	101.639
Rutter & Co.	101.59
Lamport, Barker & Jennings	100.62

The bids submitted at any other sale would show a similar divergence in ideas of value.

The difference between the high and low bid for the bonds referred to in this illustration is the difference, $3,368.64, between the premium paid by the high bidder, $4,089.08, and the premium offered by the low bidder, $720.44. Availability for sale to particular customers may account in part for discrepancies in bids.

Sources of information.—The sources of information to which the prospective purchaser and investigator may turn are statements prepared by officials of the issuing munici-

[10] The *Daily Bond Buyer*, October 21, 1921.

pality, by State officers, such as superintendents of banks, and by financial publications.

When bids are solicited for an issue of bonds, it is customary for the city officials to prepare and send to enquirers, and to publish with notice of sale, a "financial statement" showing the gross and net indebtedness, assessed valuations of taxable real and personal property, the ratio between real and assessed valuations, the tax rate, and population. Such statements, being made by the seller and by officials not always conversant with the best practice, should be carefully scanned. For an example of such statements see the summary financial statements following Chapter V.

The superintendents of banks in New York, Massachusetts, and Connecticut (alas, not in New Jersey) and other States, issue from time to time lists of counties, cities, and other political divisions, the bonds of which are "legal investments" for savings banks, trustees and fiduciaries in their respective States. A summary, compiled from such a statement issued by the superintendent of banks in New York follows Chapter XI. Such statements are valuable only in that they establish the fact that bonds of the included cities, etc., are "legal" in the judgment of and according to the best information the issuing official has been able to obtain. The omission of the name of a municipality does not necessarily mean its bonds are not "legal." It may only mean that its officials have been lazy.

The most available and the most reliable source of information is the *Commercial and Financial Chronicle,* published in New York City by William B. Dana Co. In the *State and City Supplement,* published semi-annually, complete and accurate municipal statistics may be found, together with abstracts of the laws of the various States governing the issue of municipal bonds. The greatest care is taken by the publishers to make and keep such information accurate and timely, and statements in the *Chronicle* may be relied upon.

In the last analysis, the estimation of bond prices suggests the explanation by a great painter of his brilliant colours. When asked how he mixed his paints to obtain such results, he replied: "With brains, sir, with brains."

Content of Advertisement which Appeared in the New York "Sun," November 1, 1921

Twenty Years Ago

Below is a list of municipal bonds which we owned and offered for sale during the year 1901:

CHICAGO	NEW YORK	BOSTON
204 Dearborn Street	31 Nassau Street	67 Milk Street
(*Marquette Bld'g.*)	(*Nat'l Bank of Commerce Bld'g.*)	(*Equitable Bld'g.*)

NEW YORK, 1901

We own and offer, subject to prior sale and advance in price, the following bonds:

Amount	*Name of Security*	*Rate*	*Maturing in*	*Price and Interest*	*Net Return*
$ 30,000	State of New York, Registered	3	11 Years	104	2.55
200,000	State of Massachusetts	3	38 Years	104¼	2.83
50,000	City of Boston, Massachusetts, Registered	3½	29 Years	109¼	3.03
156,000	Detroit, Michigan, School	3½	28 Years	109	3.03
200,000	Milwaukee, Wisconsin, School	3½	1 to 20 Years	Various	3.05
122,000	Buffalo, New York, Registered	3½	19 Years	106⅝	3.05
100,000	Chicago, Illinois	4	14 Years	110⅜	3.10
50,000	Newark, New Jersey, Water	4	21 Years	113⅜	3.10
50,000	City of New York, Registered	3½	27 Years	106⅞	3.12
20,000	State of Louisiana, Coupon	4	13 Years	109	3.15
100,000	State of Tennessee, Registered	3	12 Years	98	3.20
523,000	City of Allegheny, Pennsylvania, Registered	3½	2 to 25 Years	Various	3.20
125,000	Fort Wayne, Indiana, School City	3½	5 to 20 Years	Various	3.20
100,000	Greene County, Ohio, Court House	4	5 to 29 Years	Various	3.20
45,000	Blackhawk County, Iowa, Court House	4	10 Years	106¾	3.20
20,000	South Bend, Indiana	3½	10 Years	102½	3.20
100,000	Waukesha County, Wisconsin, Asylum	3.65	4 to 21 Years	Various	3.25
71,500	Rock Island, Illinois, School District	4	5 Years	103½	3.25
50,000	Clinton, Iowa, Ind. School District Refunding	4	10 Years	103½	3.25
20,000	Colorado Springs, Colorado, School District Refunding	4	20 Years	104¼	3.25
42,000	St. Joseph, Missouri, School District	4	9 to 19 Years	105⅝	3.30
38,000	Springfield, Illinois, Refunding	3½	20 Years	102⅞	3.30
25,000	Peoria, Illinois, Park District	3½	20 Years	102⅞	3.30
15,000	Danville, Illinois, Refunding School	4	8 to 10 Years	Various	3.30
26,000	Lima, Ohio, Refunding	3½	24 to 29 Years	103¼	3.30
200,000	Lee County, Iowa, Refunding	3¾	1 to 19 Years	Various	3.30
96,000	Jeffersonville, Indiana	3½	24 Years	101	3.45
25,000	Sanitary District of Chicago	4½	2 Years	102.14	3.50
25,000	Gallatin County, Illinois, Refunding	4	7 to 10 Years	Various	3.50
23,000	Council Bluffs, Iowa, Refunding	4½	14 to 15 Years	Various	3.50
59,000	County of Cascade, Montana	4	20 Years	105¼	3.63
46,000	City of Norfolk, Virginia, Imp. Refunding	4	28 Years	104	3.70
30,000	Nashville, Tennessee, Refunding	4	17 Years	103¾	3.70
125,000	City of Memphis, Tenn., Sinking Fund, Park	4	12 to 29 Years	Various	3.80
100,000	Roane County, Tennessee, Funding	4	20 Years	101¾	3.875
20,000	Bexar County, Texas, Court House	6	33 Years	105¼	3.875

SPECIAL CIRCULARS ON REQUEST

The remarkable change in price and interest return on similar representative issues in the twenty years intervening may be seen from the list of municipal bonds we now offer to yield from 5% to 6%. In some instances these are issued by the same municipalities whose bonds we offered twenty years ago. We shall be pleased to send circulars describing our present offerings in detail. We suggest you ask for List W-11.

HARRIS, FORBES & COMPANY
Pine Street, Corner William, New York

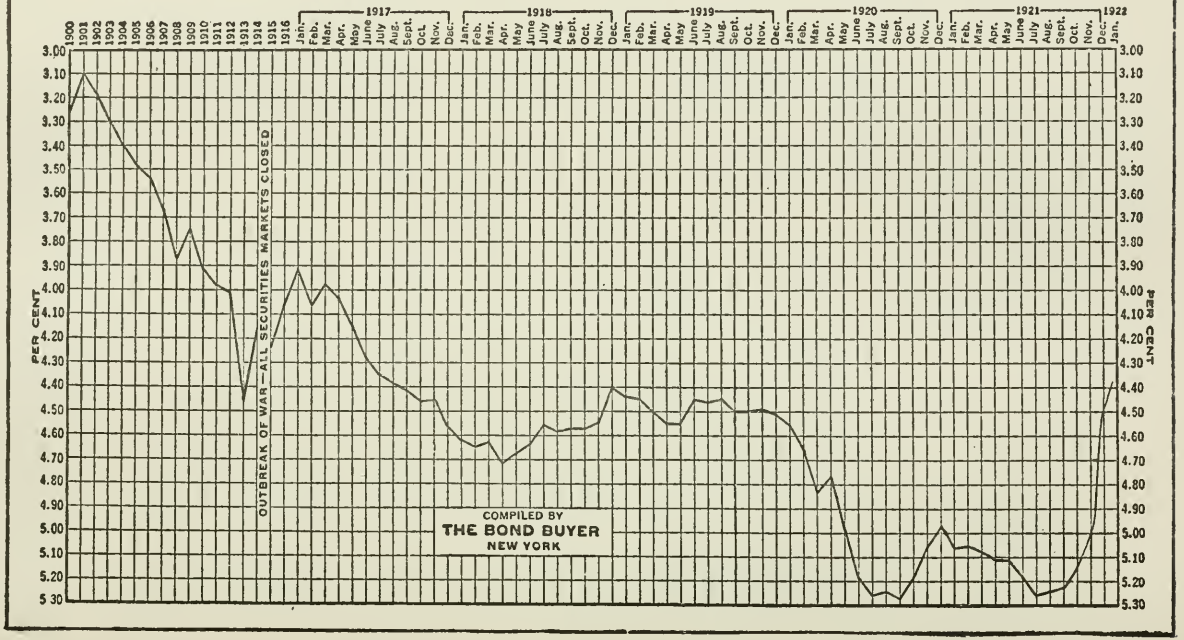
Harris, Forbes & Company
Incorporated
Boston

Harris Trust and Savings Bank
Bond Department
Chicago

The Bond Buyer's Index of the Municipal Bond Market

1900—1922

(Curve represents the average market value, expressed in net income basis, of bonds of twenty large cities in the United States.)


1900 1901 1902 1903 1904 1905 1906 1907 1908 1909 1910 1911 1912 1913 1914 1915 1916
1917 Jan. Feb. Mar. Apr. May June July Aug. Sept. Oct. Nov. Dec.
1918 Jan. Feb. Mar. Apr. May June July Aug. Sept. Oct. Nov. Dec.
1919 Jan. Feb. Mar. Apr. May June July Aug. Sept. Oct. Nov. Dec.
1920 Jan. Feb. Mar. Apr. May June July Aug. Sept. Oct. Nov. Dec.
1921 Jan. Feb. Mar. Apr. May June July Aug. Sept. Oct. Nov. Dec.
1922 Jan.
PER CENT
3.00 3.10 3.20 3.30 3.40 3.50 3.60 3.70 3.80 3.90 4.00 4.10 4.20 4.30 4.40 4.50 4.60 4.70 4.80 4.90 5.00 5.10 5.20 5.30
OUTBREAK OF WAR—ALL SECURITIES MARKETS CLOSED
COMPILED BY
THE BOND BUYER
NEW YORK

New Bond Offerings of the Week Ended Dec. 16, 1921 *

Amount	Description	Interest Rate	Term of Years	Yield Per Cent
$ 100,000	City of St. Petersburg, Fla., improvement	6	9–30	5.50 to 5.60
100,000	Richmond County, N. C., court house	6	10–30	5.25 to 5.50
2,250,000	Little Rock and North Little Rock, Ark., bridge	5–1/2	1–29	5.30 to 5.50
503,000	Harris Co., Texas, Houston Ship Channel	5	1–28	5
1,200,000	City of Lexington, Ky., municipal improvements	5	4–39	4.50 to 4.70
181,000	Stephens Co., Tex	5–1/2	3–6	6–1/4
515,500	City of Wilmington, Del	5	34–36	4.30
500,000	Allegheny County, Pa., tunnel	4–1/2	5–27	4.25
2,000,000	Mississippi Co., Ark., drainage district	6	4–21	6.25
85,000	City of Tonawanda, N. Y., school	5	2–31	4.20 to 4.75
486,000	City and County of California, water	4–1/2	3–17	4.65 to 4.80
39,000	Gloucester Co., N. J., road	6	1–5	4.80
42,000	Ocean City, N. J., improvement	6	2–12	5.20 to 5.40
1,500,000	State of Mississippi	4–3/4	3–26	4.40 to 4.70
1,200,000	City of Charlotte, N. C.	5–1/4	3–41	4.80 to 4.90
399,500	City of Calgary, Alberta	6	30–50	6
456,000	Summit Co., Ohio, road	6	2–7	4.80
80,000	City of Yakima, Wash., sewer	6	20	5.15
117,000	Town of Westfield, N. J., improvement	5–1/2	2–30	4.40 to 4.60
1,000,000	Ouachita Parish, La., road	6	1–38	5.60 to 6
3,015,000	Los Angeles City, School District, Cal.	5–1/2	2–39	4.60 to 4.90
7,360,000	City of Buffalo, N. Y., school, hospital and sewage	4–1/2	1–21	4.05 to 4.20
450,000	Yazoo-Mississippi Delta Levee District	4–1/2	5.35	5.20
1,100,000	Dunklin Co., Mo	5	3–21	5.10
55,000,000	City of New York corporate stock	4–1/2	50	4.25

* From the New York *Times*.

New Bond Offerings of the Week Ended Dec. 30, 1921 *

Amount	*Description*	*Interest Rate*	*Term of Years*	*Yield Per Cent*
$ 116,000	Duval County, Fla., bridge.....	5	37	4.875
1,264,000	City of Bayonne, N. J., school and improvement	5	3–30	4.40 to 4.60
1,500,000	State of Mississippi improvement..	4–3/4	2–25	4.40 to 4.70
2,310,000	Allegheny Co., Pa., road and bridge	4–1/2	1–30	4.15
7,000,000	State of California highway.....	5	22–28	4.30
175,000	City of Pueblo, Col., public way **	5	15	5
216,000	Sumter Co., Ga., improvement....	5	2–28	4.80
180,000	City of Portland, Ore., improvement	5	4–31	4.40 to 4.70
260,000	Springfield, Ohio, school.....	5–1/2	7–28	4.65 to 4.80
230,000	Nogales, Ariz., water.....	5–1/2	15–29	5.70 to 5.80
140,000	Carter Co., Tenn.....	6	30	5.40

* From the New York *Times.*
** Optional, Nov. 1, 1931.

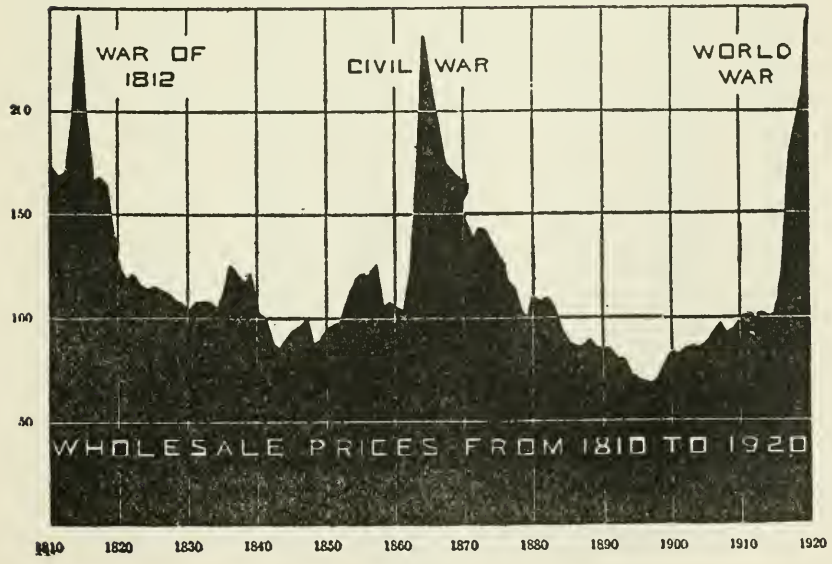
Results of New York City Bond Sales

Date of Sale and Amount	*Interest Rate*	*Years*	*Average Price*	*Income Basis*
Dec. 15, 1921				
$55,000,000	4–1/2	50	103.407	4.333
July 12, 1917				
$47,500,000	4–1/2	50	100.6507	4.46
7,500,000	4–1/2	1–15 Ser.	100.6507	4.39
April 19, 1916				
$40,000,000	4–1/4	50	102.618	4.126
15,000,000	4–1/4	1–15 Ser.	101.432	4,028
June 29, 1915				
$46,000,000	4–1/2	50	101.253	4.437
25,000,000	4–1/2	1–15 Ser.	101.306	4.297
April 15, 1914				
$65,000,000	4–1/4	50	101.45	4.18
May 20, 1913				
$45,000,000	4–1/2	50	101.137	4.49
May 7, 1912				
$65,000,000	4–1/4	50	100.747	4.214

Results of New York City Bond Sales—Continued

Date of Sale and Amount	*Interest Rate*	*Years*	*Average Price*	*Income Basis*
Jan. 24, 1911				
$60,000,000	4–1/4	50	100.904	4.207
March 21, 1910				
$50,000,000	4–1/4	20–50	101.28	4.155
Dec. 10, 1909				
$12,500,000	4	50	100.34	3.98
June 8, 1909				
$38,000,000	4	50	100.71	3.96
2,000,000	4	10	100.14	3.98
March 2, 1909				
$10,000,000	4	50	101.57	3.93
Nov. 23, 1908				
$12,000,000	4	50	102.385	3.89
500,000	4	10	101.52	3.82
Feb. 14, 1908				
$47,000,000	4–1/2	50	104.22	4.29
3,000,000	4–1/2	10	100.90	4.38
Sept. 10, 1907				
$35,000,000	4–1/2	50	102.063	4.39
5,000,000	4–1/2	10	100.30	4.46

Wholesale Prices in the United States for 110 Years



Content of Advertisement Showing Offering of $31,800,000 State of New York Gold 5% Bonds *

$31,800,000, State of New York, Gold 5% Bonds

Dated January 1 and March 1, 1921 — Due serially 1922 to 1971, inclusive

Principal and semi-annual interest payable in gold at the Bank of the Manhattan Company, New York City. Coupon bonds in the denomination of $1,000, which may be exchanged for bonds registered as to principal and interest in denominations of $1,000, $5,000, $10,000 and $50,000.

Exempt from the New York State Income Tax, and free from all Federal Income Taxes. Legal investment for Savings Banks and Trustees in New York, all New England and in other States.

Eligible as security for Postal Savings Deposits.

Acceptable to the State of New York as security for State Deposits, to the Superintendent of Insurance to secure policyholders and to the Superintendent of Banks in trust for banks and trust companies.

The assessed valuation of property subject to taxation for State purposes is officially reported as $14,850,989,607. The gross bonded debt, including this issue, is $267,729,000. Sinking funds are $76,218,877, making a net bonded debt of $191,510,123, or about 1¼% of the assessed valuation. The population, according to the U. S. Census for 1920, was 10,384,829. The outstanding debt of the State is secured by taxes levied to meet principal and interest at maturity. The present offering consists of $20,000,000 bonds for Highways, $6,800,000 for Barge Canal Terminals and $5,000,000 for the acquisition of lands for the State Forest Preserve, and matures $500,000 March 1 and $136,000 January 1 each year from 1922 to 1971 inclusive.

MATURITIES, AMOUNTS AND PRICES
(Accrued interest to be added)

Maturity	*Amount*	*Price*	*Yield About*	*Maturity*	*Amount*	*Price*	*Yield About*
1922	$636,000	99.85	5.25%	1647	$636,000	104.44	4.70%
1923	636,000	99.62	5.25%	1948	636,000	104.53	4.70%
1924	636,000	99.39	5.25%	1949	636,000	104.62	4.70%
1925	636,000	99.18	5.25%	1950	636,000	104.70	4.70%
1926	636,000	99.19	5.20%	1951	636,000	104.77	4.70%
1927	636,000	99.28	5.15%	1952	636,000	104.85	4.70%
1928	636,000	99.44	5.10%	1953	636,000	104.92	4.70%
1929	636,000	99.69	5.05%	1954	636,000	104.99	4.70%
1930	636,000	100.00	5.00%	1955	636,000	105.05	4.70%
1931	636,000	100.37	4.95%	1956	636,000	105.11	4.70%
1932	636,000	100.83	4.90%	1957	636,000	105.17	4.70%
1933	636,000	101.32	4.85%	1958	636,000	105.22	4.70%
1934	636,000	101.88	4.80%	1959	636,000	105.28	4.70%
1935	636,000	102.49	4.75%	1960	636,000	105.33	4.70%
1936	636,000	102.61	4.75%	1961	636,000	105.37	4.70%
1937	636,000	102.75	4.75%	1962	636,000	105.42	4.70%
1938	636,000	102.85	4.75%	1963	636,000	105.46	4.70%
1939	636,000	102.96	4.75%	1964	636,000	105.51	4.70%
1940	636,000	103.07	4.75%	1965	636,000	105.55	4.70%
1941	636,000	103.82	4.70%	1966	636,000	105.58	4.70%
1942	636,000	103.93	4.70%	1967	636,000	105.62	4.70%
1943	636,000	104.05	4.70%	1968	636,000	105.65	4.70%
1944	636,000	104.15	4.70%	1969	636,000	105.69	4.70%
1945	636,000	104.25	4.70%	1970	636,000	105.72	4.70%
1946	636,000	104.35	4.70%	1971	636,000	105.75	4.70%

The above information is based upon official statements and statistics on which we have relied in the purchase of these bonds. We do not guarantee but believe it to be correct.

First National Bank, New York—Bankers Trust Company—Harris, Forbes & Company—The National City Company—Guaranty Company of New York—Brown Brothers & Company—E. H. Rollins & Sons—Kissel, Kinnicutt & Co.—Potter Brothers & Co.—Bernhard, Scholle & Co.—Remick, Hodges & Company—William R. Compton Co.—Eastman, Dillon & Co.—Redmond & Co.—Stacy & Braun—Robert Winthrop & Co.

* From the New York *Sun*, June 10, 1921.

Chapter XV

INCONTESTABILITY AND VALIDATION

Improvement in civic sense of honesty.—In the merry days of reconstruction, expansion and industrial development following the war between the States, repudiation of municipal bond issues was not only frequent, but seemed in many cases not to be regarded as bad faith. However, a default in payment of interest or principal, then as now, almost invariably involved a moral default. That there has been an improvement in standards of business ethics in the last generation is a matter of common knowledge and it is gratifying to record that the civic sense of honesty leads the business sense of fair dealing. It is not that "business methods have been applied to politics," but political methods have been applied to business.

Nevertheless defaults do occur, and with sufficient frequency to keep the investment banker, the purchaser of bonds, and the skilled specialist ever on the alert. That the number is decreasing is due to many reasons, not the least being the knowledge that honesty not only is the best policy, but that honesty is absolutely essential if the municipal corporation is to continue to function. A reputation for default, even for tardiness, makes it difficult for the municipality to borrow for any purpose.

Progress on legal side.—Great progress has been made on the legal side. As municipal bonds must be authorized by statute, general or special, statutes are better drafted avoiding the errors shown by experience. Practical experience and legal skill have joined forces to produce sound and workable laws, the object of which is the protection of the investor, until today the fiscal legislation of many States in this country leaves little to be desired, either in form or substance. Among statutes of this kind are Arthur N. Pierson's Act to Regulate the Issue of Bonds by New Jersey Municipalities,[1]

[1] P. L., 1917, Chap. 240.

and William Henry Hoyt's Municipal Finance Act for North Carolina,[2] both of which have been improved and marred by subsequent tinkering.

Imperfection of all legislation.—The history of legislation, and indeed of all law, has shown that the mind of man cannot create statutes or laws which are perfect or in which the trained (not to mention the criminal) mind cannot detect flaws. This has been true with fiscal legislation. Where default has seemed advisable, necessary or inevitable to the imperfect moral sense, opportunity has not been lacking to hang the default upon the peg of illegality. To anticipate the consequences of a desire for repudiation is the business of the draftsman of fiscal legislation, and in examining such legislation we find various expedients which tend to make default difficult or impossible or assure legality of the bonds, in advance of issue.

Estoppel.—First among such devices is employment of the legal doctrine of estoppel, by which is meant that under certain circumstances we may not deny the truth or propriety of what we have previously said or done. So a municipality having the power to issue bonds, may be estopped, or prevented, by recitals in the bonds, from denying their legality. The effect of Judge Dillon's estoppel clause has been referred to in Chapter I, and the language of the clause given in the bond forms in and following that chapter. The force of such an estoppel rests upon the rule that the municipality can be bound by the agents or officers, by whom alone it can act, if they "keep within the limits of the chartered authority of the corporation." [3] The doctrine is asserted for the protection of the bondholder and ordinarily has "no place in controversies which arise before the issue of the bonds." [4]

Provision can, however, be made in advance of the issue, to give effect to estoppel. A New York statute reads: "An ordinance creating a funded debt may provide that the bonds therein authorized shall contain a recital that they are issued pursuant to law and an ordinance of the common council, as provided by section sixty of the Second-class Cities Law. Such recital, when so authorized, as aforesaid, shall be conclusive evidence of the regularity of the issue of said bonds and of

[2] P. L., 1917, Chap. 138, as last revised by an Act ratified December 20, 1921.

[3] Dillon, p. 1179.

[4] *Id.*, p. 585.

their validity." [5] And it would be so, provided that the city had the power to issue the bonds. As to irregularities in the proceedings preliminary to issue, such recital is conclusive.[6]

As questions of power are sometimes questions of limitation, some statutes provide that the determination of certain facts by certain officials shall be final. The New Jersey Bond Act provides that: "The determination of the governing body as to the classification of purposes * * * for which bonds are issued and as to the probable period of the usefulness of any improvement or property, and as to the maturities of the proposed bonds based thereon, shall, upon a majority vote of all the members of such body in office, be conclusive in any action or proceeding involving the validity of said bonds." [7] The doctrine of estoppel is invoked in advance of issue and the effect of such a statutory provision depends upon it.

Short statutes of limitations.—By a statute of limitations, sometimes aptly called a statute of repose, is meant a statutory provision that lawsuits must be begun within a stated period, longer or shorter according to the facts and character of the lawsuit or action. For example, in many States a suit brought to recover damages for breach of a contract must be commenced within six years from the time the cause of action arose. In applying such statutes in practice, the courts say in effect: "You must not sleep on your rights. If you come here for redress, you must come promptly. Otherwise, the legislature says you may not take up our time."

An application of this principle is found in the New Jersey statute so frequently quoted. After an ordinance or resolution is adopted, it is required to be published. "The clerk shall publish with such ordinance or resolution a statement in substantially the following form: The foregoing (ordinance or resolution) was (adopted or approved) on the —— day of ————————, 19—. The bonds authorized thereby will be issued and delivered after the —— day of ————, 19— (specifying a day not less than twenty days after the first publication), and any suit, action or proceeding to set aside or vacate this (ordinance or resolution) must be begun within twenty days after the publication of this statement." [8]

[5] Cons. Laws, Chap. 53, Sec. 60.
[6] Dillon, p. 1179.
[7] P. L., 1917, Chap. 240, Sec. 4 (4).
[8] P. L., 1917, Chap. 240, Sec. 2 (1) (d).

In construing and applying this provision, the Supreme Court of New Jersey said: "* * * in the absence of the protest provided for by the act, we are compelled to the conclusive presumption that the ordinance was duly and regularly passed and complied with the statute; by express statutory provision the validity of the ordinance cannot be questioned, since no action or proceeding was commenced prior to the expiration of the 20 days." [9] The presumption would not be conclusive in a case where there was no lawful authority to issue the bonds.

Validation by decree.—It has been noted in this book and by other observers [10] that the tendency of the courts is to hold bonds valid when in the hands of innocent purchasers for value, without notice and before maturity. Such a result inevitably followed the application of the Law Merchant and the Uniform Negotiable Instruments Law, to municipal bonds. Unfortunately, such adjudications follow defaults and do not precede them; and it is greatly to be desired that conclusive adjudications, determining the legality of bond issues, should precede issue. Such a result is attempted to be secured in two ways, that is, by submitting the record and proceedings, before issue, to (a) an administrative department, or (b) the courts, so that a judgment may be secured, binding not only on all parties to the proceeding, but on all those who might properly be parties, in the present and in the future. The legal doctrine of *res adjudicata* is outside the scope of this essay, but as it underlies the idea of validation by decree, it is necessary to define the term. By *res adjudicata* is meant that all questions which might have been determined in a litigation based upon the facts are so determined whether specifically presented for determination, or not, and, theoretically, at least, not only as between the parties, but as to all persons who might have been or properly could be made parties. In short, if a court says a bond issue is legal, it is so, even though all the defects in the proceedings are not brought to the attention of the court.

The effectiveness of statutes providing for such validation, that is, by administrative or judicial decree, depends upon constitutional limitations in those States where the line

[9] *Dale v. Bayhead* (1917), 90 N. J. Law 49, 100 Atl. 329; see also *Walters v. Bayonne* (1918), 89 N. J. Equity 384, 104 Atl. 770.

[10] Lagerquist, p. 575; Chamberlain, p. 236; Jordan, p. 82 and others.

of demarcation is clearly drawn between the legislative, judicial, and executive departments of government. In such States it is not competent for the legislature to impose judicial functions upon the executive, or legislative functions upon the courts.

An attempt to authorize a governmental department to exercise judicial and legislative functions in New York, where such limitations exist, has been made by the Education Law and the General Municipal Law.

The Education Law.[11]—This statute provides that a trustee, board of education, elector or taxpayer of a school district, or a purchaser of its bonds, may institute a proceeding before the commissioner of education for the purpose, among others, of "legalizing and validating the bonds" of the school district. If it appear to the commissioner of education that the proceedings taken "substantially comply" with the statute "he shall render a decision ratifying and confirming such acts and proceedings." In other words, he may say the law has been observed. But the statute goes on to say: "If there has been a fair expression of the will of the qualified electors of the district, and it appears that the action taken was not affected or prejudiced by defects in, or failure to give, the notice required by statute, or if it appears that the failure to take, or a defect in any step in the acts or proceedings of district officers or meetings did not influence materially, the result of such meetings, the commissioner may disregard such defects or failure and determine that there has been a substantial compliance with the statute."

The statute has not been passed upon by the courts, but in view of the principle stated above, and the language of the Supreme Court in the *Lackawanna* case hereafter referred to, it is to be assumed that the attempt to vest the commissioners of education with judicial functions is unconstitutional.

The General Municipal Law.[12]—This statute provides for a proceeding in the Supreme Court, based upon a petition made by interested parties (that is, municipal officials, taxpayers, purchasers or holders of the bonds) setting forth all facts in relation to the bond issue "for the purpose of legalizing and confirming such proceedings * * * and also the issuance, sale and form of such bonds." The court is given juris-

[11] Cons. Laws, Chap. 16, Sec. 480, sub. 7, added by Laws of 1917, p. 1276.
[12] Cons. Laws, Chap. 24, Secs. 22 to 29.

diction to determine that the statute authorizing the bonds "was substantially complied with" *if* certain conditions specified in the act have been complied with, "notwithstanding any irregularity or technicality" mentioned in the act.

In construing this statute in the *Lackawanna* case [13] the court said: "There is, then, found in 'the statute' a simple and comprehensive legislative scheme whereby the legislature has declared in substance that all municipal bond issues shall be valid, wherein the sole objection thereto lies in certain specified and defined technical irregularities, and whereby there is committed to the Supreme Court the *purely judicial function of determining in each instance where the statute is involved the question of fact* [14] of whether there are or not any other irregularities than those mentioned in such statute. It is thus made clear that the bond issues acquire their validity solely from the legislative enactment and not from the court, and there is, therefore, no legislative function committed to the court." In other words, if the bonds are authorized by the statute and the proceedings are regular, the court may say so, but it has no jurisdiction to declare the bonds legal, if they are not.

The two preceding illustrations are given to show the difficulties of validation by decree where the State constitution contains inhibitions. In the words of the Bishop of Rum-ti-foo: "No; that is a length to which, I trow, Colonial Bishops cannot go. You may express surprise" to find that there are constitutional limits to legislation. Legislative draftsmen and legislators frequently find it is so.

Judicial validation in Georgia.—In Georgia, however, as in France "they order this matter better," or at least a constitutional, workable scheme of judicial validation has been enacted. This statutory plan in substance is as follows: [15]

When a proposition to issue bonds has been adopted at an election, notice is given to a designated State official, who begins an action against the county or municipality which desires to issue the bonds. An order is obtained directing the county or municipality to show cause "why the bonds should not be confirmed and validated." A hearing is had and determination made as to "all the questions of law and of fact."

[13] *Matter of Lackawanna* (1913), 158 App. Div. 263.
[14] Italics mine.—F. B.
[15] Civil Code 1910; Sec. 445 *et seq.*

If the proceedings are approved, and there appears to be no difficulty about it, for the defendant municipality or county wants the bonds issued, a judgment is entered. The effect of such judgment is "forever conclusive upon the validity of the bonds against the county, municipality, or division, and the validity of said bonds shall never be called in question in any court" of the State of Georgia.

An objecting taxpayer can intervene in the action and attack the regularity of the proceedings. The act requires due notice, constructive but nevertheless legally sufficient, and is sound in principle.

Judicial validation sustained.—Such validation has been sustained. A typical instance of litigation in which the constitutionality of the statute was sustained by inference and a possible default prevented, is *Dumas v. Rigdon*.[16] Certain taxpayers of Tift County, Georgia, sought to restrain the collection of a tax levied for the purpose of paying the principal and interest of bonds of the Chula School District, on the ground that the district had never been legally created.

The bonds were issued in 1918, shortly after the district was laid off by the county board of education, and the order validating the bonds was made in August, 1918.

In support of the application for an injunction, it was alleged: "that the entire territory of Tift County has never been laid off into school districts, nor have the district lines been defined and marked as required by law, nor have the school districts been laid off according to law, but they have been laid off in disregard of the provisions of the statutes upon that subject; that no map of the county showing the school districts, as required by law, has been made; that certain specified lots were illegally transferred to the Chula district: that several lots in the county were not in any school district, and that some four or five lots, containing an aggregate of some 2,000 acres of land, were illegally taken from the Chula district; that, upon other grounds specified, a division of the county into school districts, if ever made, was illegally made, without reference to best interest and the convenience of those who were included in and excluded from the district; that the territory from which the tax is to be collected is incapable of exact determination, never having

[16] (1921), 151 Ga. 267, 106 S. E. 261.

been exactly laid out, marked, and defined, as required by law."

The Georgia Supreme Court, sustaining the judgment of the lower court refusing an injunction, said:

"The bonds in question were duly validated in accordance with the provisions of the Civil Code 1910, Sec. 445 *et seq.*, relating to bonds and their validation. Questions of whether the law in regard to laying off the country into school districts had been complied with, and whether other steps were taken by the proper county authorities to make this laying off and division of the county into school districts conformable to law, as embodied in section 1531 *et seq.*, of the Civil Code, upon the subject of school districts and local tax for public schools, could and should have been made in the proceedings to validate the bonds, the legality of which is now challenged."

Registration.—Differing from validation by decree, more in form than in substance, is registration of bond issues with public, usually State, officials. Registration in this sense is not the same in its legal effect as the registration referred to in Chapter II. When a bond is registered with a public official, it is presented to the official and a notation in a proper record book is made, describing the bond by its number, date, purpose, maturity, interest rate, and other details. Such registration is intended to preserve a public record of the issue of the bonds. The effect of such registration depends upon the statute pursuant to which the bond is registered. The constitutional difficulty above referred to may exist as to registration of this sort, but assuming it does not, the registration is of two kinds:

(a) Where judicial functions are performed by the registering official, in which case registration may be conclusive as to validity (or not) according to the statute;

(b) Where ministerial functions only are performed, that is, there is no discretion with the registering official, in which case registration ordinarily does not validate the issue.

"The effect of registration pursuant to statute," says Judge Dillon, "is to be determined by the language and intent of the enactment. If from a consideration of the language used, and a reasonable construction thereof, it appears that the legislature intended to entrust to an officer the duty of determining the validity of the bonds before registering them, his certificate of registration is an adjudication of validity

which operates as an estoppel. If, however, the statute expressly declares that registration and the certification of the officer shall not have this effect, or that the certificate shall only be *prima facie* evidence of the facts stated and shall not prevent proof to the contrary in any suit involving the validity of the bonds, or the power and authority of the municipality in whose name they are executed, to issue them, all conclusive effect must be denied to the registration and the certificate." [17]

It should be noted that if the statute pursuant to which bonds are issued, requires registration and certification as a condition precedent to validity, such registration and certification is essential to the complete execution of the instruments so as to bind the municipality for their payment.[18]

Certification of signatures and seal.—If a bond is stolen before it has been issued by the municipal authorities, it has no legal inception, and it is inoperative even in the hands of a *bona fide* purchaser for value.[19] Hence if a blank bond which is ready for execution but has not been executed, is stolen and the signatures and seal forged, the municipality is not liable, except possibly where the facts show gross negligence, in which case the recovery, if any, would be because of such negligence. The condition of the law in this respect is comforting to the municipality, but would hardly add to the happiness of an innocent holder for value of forged securities.

Forgery is an ever-present and real menace, as everyone knows who has to deal with securities. How is the purchaser to know the bonds he buys are genuine? At the time of issue there is no particular difficulty, because executing officials are identified and signature certificates provided and made by trustworthy bank officials. But a signature certificate cannot readily be made for each bond and delivered with it as the bonds are retailed.

The United States Mortgage and Trust Company of New York, and institutions in other parts of the country, meet this difficulty by endorsing their certificate on each bond, that the signatures and seal are genuine. Elaborate precautions to guard against forgery are taken by the bank mentioned, which requires that bonds be printed or engraved under its super-

[17] Dillon, pp. 1520 to 1522.
[18] *Id.*, p. 1272.
[19] *Id.*, p. 1546.

vision, on its specially prepared water-marked paper. The utmost care is exercised to see that the officials are properly introduced and identified. Lastly, this bank must know that counsel has approved the proceedings, before it permits the executed pieces out of its possession.

In considering the subject and the contents of this chapter, the author is reminded of the many expedients proposed to end the World War, such as Henry Ford's peace ship, which was to "get the boys out of the trenches by Christmas." All devices to make bonds incontestable and to validate them before issue are to some degree expedients and where statutes require action to this end before issue, an additional burden of compliance with formalities is placed upon municipal officials and examining counsel. Everything considered, no device or expedient takes the place of adequate statutes and strict compliance with the requirements of the enabling acts.

Chapter XVI

PARTICULAR BONDS

Bonds classified.—It has been pointed out that there is a difference between bonds issued by a city and those issued by a school district; in other words, there is a difference between bonds with regard to the issuing political unit. This difference arises because the powers of the issuing bodies differ not only as between themselves, but as between classes. There is a difference between bonds considered in relation to the purposes for which they are issued and as to method of payment. In the following pages the salient features are pointed out, of city, county, and tax district bonds, of bonds issued for various purposes and of bonds having different tax means of payment. Much will be a summary of principles, and much that is said depends upon the application of general principles.

City bonds.—Cities have, by virtue of their charters, more or less complete self-governmental power, according to their size, geographical location, and commercial importance. The city is expected to have full and complete powers of taxation and it also has incidental powers, such as the power to borrow money in anticipation of its revenue. It is because of this that bonds of a city are relatively better supported than are bonds of the minor political subdivisions. To a lesser extent this is true of towns, villages, and boroughs. A city is, and must be, a going concern and should always maintain its credit, in order that it may borrow in anticipation of taxes to pay running expenses and to meet emergencies. Cities have large general powers to raise money, have funds on hand available to pay the interest on, and maturing principal of, their obligations, and then are more businesslike in making provision for maturing debts, than less highly organized political subdivisions.

County bonds.—Considered from the angle of the issuing political unit, county bonds must be separately classified, as pointed out in Chapter III. Counties are in a class by them-

selves, being major political subdivisions of the State, with many municipality powers, but not true municipal corporations. There is no difference in the eyes of the law, between bonds of a county and a city, but there is a very practical difference, for the reason that the purposes for which counties may issue bonds are relatively few in number and the total amount of bonds issued is small in proportion to the total assessed valuation of taxable property in the county.

In many States, county taxes are more certain of payment than taxes of a city or town, because of the plan of collection. Thus, the county taxing or budget-raising body determines the amount of the annual county budget, apportions the amount among the included municipalities, and other taxing units, and notifies them of the respective amounts to be raised. The various municipalities must find the money and pay their share into the county treasury, even though they are obliged to borrow for the purpose before the taxes are collected.

It will be remembered that the county debt statement is misleading and for the purposes of comparison of debt between counties, the debts of included subdivisions, such as cities, towns and villages should be considered. Another factor which we rarely take into account is contingent liability for the debts of included subdivisions. A county may pledge its credit on behalf of a tax district. Even though the property in the tax district is primarily liable to a tax for the payment of the bonds, a secondary liability arises if there is a default, which is no less real, although difficult to enforce.

Bonds of minor municipalities.—The names, *village, borough, town,* and *township,* suggest minor political units, having less complete powers of government than cities. As with county bonds, there is no difference in contemplation of law between the bond of a city and the bond of a village, but nomenclature is important. Many villages are larger and wealthier than some cities, but the bonds of a city may be "legal investments" under the laws of a State, while the bonds of a village may not be. *Village, borough,* and *town* suggest small populations, rural communities, low valuations of taxable property, and lack of manufacturing and commerce.

Bonds of tax districts.—Familiar illustrations of tax districts are irrigation, levee, and drainage districts, and in some States, water and sewer districts. While bonds of such districts are not, strictly speaking, assessment bonds, the theory

upon which taxes are levied and raised is that the property included in the district is increased in value by the improvement and that the increase in value may be taxed to pay the bonds issued therefor. The scheme of taxation will be considered hereafter in the paragraph devoted to irrigation district bonds.

Tax districts, whether called irrigation, sewer, drainage, or fire districts, are created for one purpose, to provide one utility or pay for one project. Hence if the project fails, there may be no value to tax, or the collection of taxes may be resisted. There is usually no general power of taxation in the board or body issuing the bonds and no collateral or other means of remedying a default. The district has no independent funds or credit, and if its taxes are not collected, its bonds may be and probably will be valueless.

Purpose of issue.—Considered as to purpose, bonds may be divided into those issued to provide more or less self-sustaining public utilities, and those issued to acquire property from which there is no direct return to the municipality, such as parks and streets. In the first case, the municipality secures an income from the operation of the improvement or utility. In the second case, taxable valuations are enhanced, a decided benefit ensuing from the completion of the improvement or acquisition of the property.

Bonds for necessary public purpose.—Water bonds are regarded as being issued for an absolutely necessary public purpose. Hence we find that, by virtue of constitutional or statutory provisions, they enjoy the privilege of being outside most debt limits. In addition to being supported by the power of direct taxation, a well-managed municipal water works system should, and usually does, produce enough revenue by way of water rent or meter charge, to pay the operating expenses and the interest and principal on the bonds issued therefor. As observed in Chapter VIII, this is especially true of a system operated by gravity. If the water system is operated by pumping, the expense of operation is largely increased and the resulting revenue may or may not be large enough to take care of debt service. Much also depends upon the municipal bookkeeping, which is not always as exact as corporate bookkeeping, for the reason that city officials like to make as good a showing as possible. Municipal operation (not municipal ownership) is by no means free

from waste, and municipal bookkeeping does not always tell the true story, for obsolescence and wear and tear, as well as other items, may not be shown and provided for.

In computing indebtedness for various purposes, water bonds are ordinarily deductible because, the income being sufficient to take care of debt service, there is no direct tax burden upon taxable property. These principles apply to a greater or less extent to all public utility issues where there is a direct income derived from the utility. Among other bonds of this kind may be mentioned those issued to acquire markets, wharves, docks, and electric lighting and power systems. Public utility bonds of other kinds may or may not be regarded as self-liquidating and hence as having an additional factor of safety.

Sewer systems are sometimes made to produce a direct operating income. This is very unusual and wherever it is observed, it is probable that the charge is made for the purpose of avoiding a direct tax and thus keeping the bonds out of the gross indebtedness.

Bonds to provide properties and improvements.—Bonds to provide properties and improvements which produce no direct revenue are those issued to purchase parks and improve streets. Such improvements and many others do, however, indirectly increase the municipal revenues because they enhance taxable valuations. For example, a house and lot, assessed at a valuation of $10,000 produces an annual tax return of $250 if the rate is $25 a thousand. The construction of a well-paved street, or a sewer may increase the value of the property to $15,000, in which case the tax return at the same rate is $375 or an increase of $125 a year. Such an income economists call service income.

School district bonds have a great sentimental value in this country, where education is regarded as of primary importance. A school district will not willingly default, for the educational needs of a growing population must be met. Local pride is not quite the same as good faith, but is a fair substitute for it.

Irrigation, drainage and levee district bonds are issued to provide funds for a particular public improvement which, if successful, enhances the taxable valuation of the benefited property to such an extent that taxation for debt service may be lessened, and certainly the increase, if any, should not be

an appreciable burden. If the improvement is a failure, there is, in many cases, not a sufficient increase in taxable valuations of property to permit the levy of taxes large enough to provide interest and principal. The theory of taxation under most statutes governing the issue of bonds of this class, is that the improvement, when completed, will increase the taxable valuation of the real property included in the district and that this increase may be taxed. This increase, for the purpose of illustration, may be from $250,000 to $1,000,000, or an increase of $750,000. If the annual charge for maintenance of the project and for debt service is $5,000, the annual tax is 6 2/3 per cent of the increase in value. Hence if a farm valued at $5,000 is increased in value to the extent of $2,500, the additional tax will be $16.35.

Means of payment.—Classified as to means of payment, we have on the one hand the direct obligations of the municipality, payable from the proceeds of a general ad valorem tax on real property, and assessment bonds on the other. For a discussion of assessment bonds, the reader is referred to Chapter VIII. An additional factor to be noted is uncertainty of collection of assessments because of lack of clearness in the statute authorizing the levy of the assessment. Another factor of uncertainty arises from the difficulty existing under the constitutions and statutes of many States, of proving that the property has in fact been benefited to the extent claimed. Again, if the project is a failure, or only partially successful, owners of property alleged to be benefited frequently make determined efforts to avoid the payment of the assessment and such efforts are in many cases successful. Prolonged and expensive litigation not infrequently follows the issue of assessment bonds. In the eastern States assessment bonds are usually the direct obligation of the issuing cities and stand on no different footing from any other bonds as between the city and the bondholder. As between the city and the property owner, the latter must pay, but the bondholder need not look directly to the property owner.

Assessment bonds may not be negotiable instruments, because payable from a special fund and hence are not, for reasons heretofore given, to be regarded as highly as bonds which are negotiable instruments in fact.

Electoral bonds.—Electoral bonds are only important as evidencing popular assent to the issue. No consideration has

been given in this book to municipal elections, although in many jurisdictions, bonds cannot be issued except after an election has been called and held, and a majority of the voters have expressed their consent. The author regards elections on bond issues as being really limitations on the power to issue and as such only justifying consideration in particular cases and not justifying extended discussion in a book devoted to statements of general principles. As a matter of fact, the municipal taxpayers' election is an extremely clumsy expedient, intended, it is true, to secure an expression of popular opinion, but operating as a limitation of power upon duly constituted public officials. The most that can be said of elections on bond issues is that they show the attitude of the mind of the taxpayer at the time of the election, and hence it may be said that electoral bonds indicate popular assent.

Chapter XVII

THE ATTORNEYS' FUNCTIONS

Law defined.—Charles Dickens, in what is probably the greatest novel in the English language, and certainly the greatest legal novel, says that the great business of the law is to make business for itself, and that when viewed thus, it is a consistent scheme and not the mere tangle that the laity are apt to think it. When Dickens wrote at white heat, denouncing abuses, as he did in his greater novels, he was not always considerate of other people's susceptibilities, and not always just.

Law is in reality nothing but rules of human conduct applied to the game which we call life. While it is true that lawyers make the rules we call law and apply them in practice, it must nevertheless be remembered that it is the frailty of the human conscience and the human understanding which has made rules necessary. It has been well said by Pollock that the genius of English law is to make self-help unnecessary. In other words, law aims to throw disputes into the courts for an orderly settlement. But it should be borne in mind that the best work of lawyers is done outside of the courts, and that this work is the most valuable to the client.

Application of law to municipal financing.—Municipal financing, or rather municipal borrowing for capital expenditures, is of comparatively recent origin. In this country it may be said to date from the days of expansion and reconstruction following the war between the States. It has taken some time and a great deal of experience to produce fair and equitable rules by which the game may be played. While we cannot say that these rules are settled, they are at least in process of becoming definite. Until rules governing the issue of municipal securities become firmly established and well understood, the intervention of the lawyer, expert in the subject, will probably be necessary.

In view of the fact that municipalities can be sued and their contracts are enforceable in the courts, it is very neces-

sary to know the legal provisions under which municipal and other civil loans are issued, if investments in the securities are to be safe. To be valid obligations, the loans must be issued in accordance with these provisions, which may be contained in State constitutions, general statutes, or in municipal and local ordinances applying directly to the loan. Certain attorneys specialize in furnishing opinions on the legality of municipal bond issues, and no issue should be placed on the market without procuring a reliable opinion as to its validity. The purchaser of bonds should be assured by competent and reliable authority that the legal provisions relating to an issue of municipal bonds have been fully complied with.

Questions of legality.—Questions of legality may be properly classified as, first: questions as to the power to issue and to pay the bonds, and second: questions as to procedure.

Power to issue and to pay bonds.—The existence of the power to issue the bonds and to levy taxes for their payment must be determined as a matter of law before issue, for estoppel and the protection afforded the innocent holders of negotiable paper are of no avail if these powers are lacking. If the bonds are infirm in these respects at the time of issue, they continue to be infirm, except as legislatures may afford relief.

Questions as to procedure.—In the second classification, we find infirmities of procedure, such as the irregular adoption or publication of the ordinances authorizing the bonds, or failure strictly to comply with statutes requiring par sale after public notice. Generally speaking, such defects become *de minimus* as soon as the bonds reach the hands of a holder for value without notice. Irregularities of procedure may afford ground for a taxpayer's suit to restrain the issue, and for this reason may be troublesome. And it is always difficult to establish when, as a matter of law, the bonds have reached the haven where they are safe from attack.

Bondholders protected by U. S. Supreme Court.—"In municipal bond cases, the Supreme Court of the United States has rejected, when necessary to protect the *bona fide* holders of such securities, narrow and rigid constructions of statutes and charters authorizing the creation of such debts. Against such holders, it has given no favour to defenses based upon mere irregularities in the issue of the bonds or upon noncompliance with preliminary requirements, not going to the

question of statutory power to issue them. It has held that the Circuit Courts of the United States were clothed with full authority, by *mandamus* or otherwise, to enforce the collection of judgments rendered therein on such bonds, and that this authority could not be interfered with to the injury of the creditor, either by the legislature or the judiciary of the States. It has upheld and protected the rights of such creditors with a firm hand, asserting the jurisdiction and authority of the Federal courts with such striking energy and vigour as apparently, but not actually, to trench upon the lawful rights of the States and the acknowledged powers of the State tribunals. Upon the whole, however, there is little doubt that its course has had the approval of the profession in general and of the public, and the result ought to teach municipalities the lesson that if, having the power conferred upon them, they issue negotiable securities, they cannot escape payment if these find their way into the hands of innocent purchasers. The result, moreover, has been of incalculable value to municipalities in general by establishing upon a firm foundation the credit of their securities issued for needed permanent improvements, enabling them thereby to obtain money for these purposes on a lower interest basis than would otherwise have been possible. And for this the country at large is under lasting obligations to the wisdom, courage, foresight and sense of justice of the Supreme Court of the United States." [1]

Questions as to legality.—As most questions in regard to legality, which are serious, are questions of power, it has become usual for municipalities to retain expert counsel before any proceedings are started. The facts are submitted and questions of power determined, and problems of procedure resolved. The specialist will prepare the ordinance and necessary resolutions, and will advise the municipality as to the procedure to be followed, and when the bonds are to be sold, the notice of sale will usually state that an opinion of counsel will be furnished without cost to the successful bidder. This plan ordinarily results in the purchaser being able to obtain the bonds within a very few days after the award, and before market conditions have materially changed.

In commenting upon litigation between a western county and a well-known investment banking house, in which case the

[1] Dillon, p. 1402.

purchaser's attorneys declined to approve the legality of the bonds, and the purchaser was sustained by the courts, the editor of the *Bond Buyer* has recently said:

"Every one of these cases is a powerful argument in favor of approval of bonds by recognized bond attorneys *in advance of the original sale.* The municipality which does not offer the purchaser of its bonds the approving opinion of a recognized bond attorney is taking an entirely unnecessary risk of being seriously delayed with its public improvements, or worse, financially embarrassed if its loan happened to be for the purpose of meeting a maturing obligation.

"It has been conceded long ago by many large municipalities that the cost of the attorney's opinion is recovered in the enhanced price the bonds will bring over the price the dealer will bid for bonds not approved in advance, since the delay incident to having the legality investigated is, at least, equally as disadvantageous to the buyer as it is to the seller."

When the purchaser retains counsel.—In cases where the municipality does not retain counsel, the purchaser must, of course, do so. The bid should be conditioned upon the furnishing to the purchaser of a record of proceedings, showing that the bonds have been regularly issued to the satisfaction of the purchaser's attorneys. This course entails delay. Counsel must be advised of the nature of the issue, make a preliminary statutory search, then write a letter calling for papers, examine them and probably be obliged to make additional requests for information. It is obvious that this course must inevitably result in delay, and that the market may fall between the time of award and the time the opinion is forthcoming. If counsel fails to approve the issue, the bond house must pay its lawyers and charge off the fee to its lost-bond account. The municipality is quite apt to charge the purchaser with bad faith, and to intimate that counsel have allowed themselves to be influenced by market conditions or their clients' desires. This is never so with reputable attorneys, but it is very difficult to substantiate such a denial. The courts have, however, said in several cases and we may regard it as settled law, that in the absence of a showing of bad faith or gross negligence, a bond house will not be compelled to take securities which are not legal in the opinion of its counsel, provided the bid contains the proper condition, that is,

that the legality be evidenced satisfactorily to the purchaser's counsel.

The record of proceedings.—A record of proceedings must be obtained in order to enable counsel to form an opinion as to legality. This record consists of a large number of papers intended to show who are the city's officers, the proceedings taken to issue the bonds, and the certificates necessary when the transaction is completed. It is much easier to obtain a proper record before sale than after it; there is more time and there has been less opportunity for bad blood to develop. Quite frequently counsel asks for papers, the relevancy of which is not apparent to the municipal official who must prepare them, but as an attorney engaged in this class of practice once said, "If I ask for the picture of the city clerk's mother-in-law, I want it and I do not want any request for an explanation." The point is, that counsel must form an opinion and express it in writing. He must have facts before him on which to predicate an opinion and different attorneys invariably differ as to the proper contents of a record.

At the end of this chapter is a copy of a "Record Memorandum" showing the papers necessary to form a record of proceedings in regard to a typical bond issue. Following that is a "Memorandum for Examination of Municipal Bonds," which shows the nature of many of the questions which must be disposed of by the skilled specialist.

The opinion.—It is becoming the practice for counsel to give two opinions, one called preliminary and the other final.

The preliminary opinion means that all essential papers have been passed upon, and that when certain additional steps are taken, an unqualified approving opinion may be forthcoming. It concludes as follows:

> Said bonds may be taken up and paid for and we will give our final approving opinion when we have examined a form of said bond and are furnished with formal proof that,
>
> (a) the signatures upon said bonds are genuine,
>
> (b) said bonds are taken up and paid for in accordance with the contract of sale.
>
> Yours very truly,
>
> .....

The final opinion is similar in form to the preliminary opinion, except that the bonds are described "as" instead of

"to be" issued, "are" instead of "will be" binding obligations, and is as follows:

February 8, 1922.

Hon. William J. Wallin,
Mayor of the City of Yonkers,
Yonkers,
New York.

Dear Sir:—

We have examined a record of proceedings relating to nine issues aggregating $2,312,000 of coupon bonds of the City of Yonkers, a municipal corporation of the State of New York, dated January 1, 1921, exchangeable at the option of the holder for bonds registered as to both principal and interest as follows:

$25,000 Department of Public Works Equipment Bonds, numbered from 1 to 25 inclusive, maturing $5000 on January 1 in each of the years 1922 to 1926 inclusive;

$300,000 Assessment Bonds, numbered from 26 to 326 inclusive, maturing $50,000 on January 1 in each of the years 1922 to 1927 inclusive;

$14,000 Public Building Bonds, numbered from 326 to 339 inclusive, maturing $1000 on January 1 in each of the years 1922 to 1935 inclusive;

$60,000 City Hall Bonds, numbered from 340 to 399 inclusive, maturing $3000 on January 1 in each of the years 1922 to 1941 inclusive;

$1,070,000 Local Improvement Bonds, numbered from 400 to 1479 inclusive, maturing $53,500 on January 1 in each of the years 1922 to 1941 inclusive;

$154,000 Dock Bonds, numbered from 1480 to 1639 inclusive, maturing $7700 on January 1 in each of the years 1922 to 1941 inclusive;

$460,000 School Bonds, numbered from 1640 to 2099 inclusive, maturing $23,000 on January 1 in each of the years 1922 to 1941 inclusive;

$149,000 Grade Crossing Elimination Bonds, numbered from 2100 to 2259 inclusive, maturing $7450 on January 1 in each of the years 1922 to 1941 inclusive;

$80,000 Water Bonds, numbered from 2260 to 2339 inclusive, maturing $2000 on January 1 in each of the years 1922 to 1961 inclusive;

All of said bonds bearing interest at the rate of five and one-half per centum (5½%) per annum, payable semi-annually on April 1 and October 1 in each year and at maturity, issued pursuant to the Second Class Cities Law and Chapter 452 of the Laws of 1908 as amended, and in the case of the Grade Crossing Elimination Bonds pursuant to the Railroad Law, and in the case of the School Bonds pursuant to the Education Law of the State of New York, and pursuant to ordinances of the City of Yonkers, approved December 29, 1920, and in our opinion said bonds are binding and legal obligations of the said City.

We have examined bonds No. 1, 26, 326, 340, 400, 1480, 1640, 2100 and 2260 of said issues and in our opinion the forms of said bonds and their execution are regular and proper.

Yours very truly,

.....

Such an opinion means just what it says, namely, that the bonds are binding and legal obligations of the municipality. Legal or legality means something more than the mere formality of issue; it means the expression of a perfect obligation; it means that the security of the obligation and the means of payment are such that the buyer need have no concern about his income and investment. Among other things, it means that the power to issue the bonds exists, that they are within every statutory and constitutional limitation of indebtedness, that every step required to be taken has been taken in due time, form and manner, and that sufficient tax may be levied to provide funds to pay the bonds.

Qualified opinions.—It is occasionally necessary to give qualified opinions. This necessity arises because there is a limitation upon the taxing power, and sometimes because there has been a failure of procedure. A characteristic qualification where there is a limited tax is the following:

> In addition to the tax of ½ of 1 per cent for general purposes, the city is authorized to levy an additional tax not exceeding ¾ of 1 per cent per annum upon the value of the taxable property therein to be devoted to the payment of its public debt and the interest thereon and to the maintenance of its public schools and public conveniences.

A limitation expressing a failure fully to comply with the statutory requirements is contained in the latter part of an opinion:

> Notwithstanding that the right to attack the validity of said bonds has not been cut off, as provided by the statutes of New Jersey, the said bonds are in our opinion binding and legal obligations of said Township.

As an example of an opinion intended clearly to express the true character of the bonds, the following is of interest:

> In our opinion, said bonds will be binding and legal obligations of the Town of Mamaroneck, payable in the first instance from assessments and not from a general town tax, which, however, can be levied if there is a shortage in the primary fund.

When a qualified opinion is merchantable.—It is quite unusual for a qualified opinion to be merchantable, though occasionally such an opinion may be used. The investment banking houses require unqualified opinions.

Whether an opinion is merchantable or not depends largely upon whose opinion it is; the attorney must be gen-

erally recognized as a specialist and expert before his opinion will pass current. It is, of course, true that opinions of certain attorneys are merchantable in some parts of the county and not so in others, and some attorneys will approve certain classes of securities which others will not approve. An opinion by counsel whose name is well-known presumably makes it easier for the purchaser to sell the bonds and the sophisticated purchaser demands such an opinion.

"One of the strongest influences making for the present admirable credit of American municipalities has been the scrupulous care with which all questions affecting legality have been considered. To attempt an estimate of the proportion of all loans that have been put out with sufficient irregularity to cause correction by attorneys before acceptance, would occasion unnecessary alarm. The bond attorney stands between the taxpayer and the investor, protecting each against the other, and working in the interest of both for a still higher development of municipal bond law and bond practice. His work is now so well done, and so systematically, that we rightly take it as a matter of course, and give ourselves, as individual buyers, in dealing with bond issues of recent years, to other considerations than those connected with validity." [2]

[2] Chamberlain, p. 234.

Form of Record Memorandum

NEW JERSEY PERMANENT SERIAL BONDS

(FOR OTHER THAN SCHOOL PURPOSES)

RECORD MEMORANDUM

Prepared for the assistance of clients by
HAWKINS, DELAFIELD & LONGFELLOW,
ATTORNEYS AT LAW,
20 Exchange Place,
New York City,

March 1, 1921.

This memorandum is intended to be helpful in the preparation of a record of proceedings upon which an opinion approving bonds can be based. The proof referred to is not necessarily complete, and it should be understood that it is generally necessary after examining such proof to ask for additional papers.

As a preliminary matter and for the purpose of determining the maturities of the bonds and the character of the ordinance to authorize them, the following information should be furnished, and, if the bonds are for several purposes, this information should be put in tabular form:

(*a*) A description of each improvement made or property acquired, that is, its kind and location, which description should be sufficiently definite to enable its classification to be determined within the definition of the Pierson Bond Act. (*Sec. 4, (2) as amended 1917, Chap. 240, p.804.*)

(*b*) The date when the improvement was completed or the property acquired. (*Pierson Bond Act, Sec. 4 (3), as amended 1917, Chap. 240, p. 806.*)

(*c*) The amount of the cost to be paid by the municipality at large.

(*d*) The date the last installment of the assessment is payable. (*Pierson Bond Act, Sec. 2 (1) (a), as amended 1917, Chap. 240, p. 804.*)

(*e*) The amount of uncollected assessments.

(*f*) The total cost of the improvement.

(*g*) Amount of temporary notes or bonds outstanding.

If there are no assessment improvements involved, items (*c*), (*d*) and (*e*) should be omitted.

The following are the papers to be included in the record of proceedings:

1. A certificate by the Clerk covering the following matters:

(*a*) The names and dates of election or appointment and dates of commencement and end of the term of office of the members of the governing body, the chief financial official (stating the name of his office), the Clerk, the Treasurer, and of the other officials, if any, who will execute the proposed bonds.

(*b*) An extract from the rules of order or resolution of the governing body which fixes the times for its regular meetings. If this cannot be furnished, the times at which the regular meetings are held should be stated.

(*c*) If the municipality is governed by the Walsh Act, a statement that at an election held on a certain date, stating the date, a majority of the legal voters assented to an Act of the Legislature of the State of New Jersey entitled: "An act relating to regulating and providing for, the government of cities, towns, townships, boroughs, villages, and municipalities governed by board of

commissioners or improvement commissions in this State," approved April 25, 1911, by the following vote:

For the adoption (state vote)
Against the adoption (state vote)

(*Walsh Act, Sec. 18, as amended by P. L. 1915, p. 12.*)

Also a statement, if it be the fact, that no election in the municipality has been held on the question of whether it shall abandon its organization under the said act (*Walsh Act, Section 19 as amended by P. L. 1917, p. 146*) and that the municipality is organized and acting thereunder.

(*d*) If the municipality is not governed by the Walsh Act a reference to the act which prescribes its form of government. If the city is acting under a referendum act proof of its adoption must be furnished.

(*e*) A statement of the corporate name of the municipality, and if it be the case, a statement that the corporate name of the municipality has not been changed by any election or shortened by any resolution. If the corporate name has been changed by an election, a copy of the minutes recording the results of the election should be set forth. (*Act Concerning Municipalities, Art. II, P. L. 1917, p. 320*). If the corporate name of the city has been shortened, a copy of the resolution of the governing body relating thereto should be set forth. (*Act Concerning Municipalities, Art. III, P. L. 1917, p. 321.*)

(*f*) A statement of the official newspaper or newspapers of the municipality. (*Act Concerning Municipalities, Art. XXXVII, Sec. 4, P. L. 1917, p. 456.*)

2. If the corporate name of the municipality has been changed by an election, a copy of the minutes recording such election as filed in the office of the Clerk of the County certified by such Clerk, and also a copy as filed in the office of the Secretary of State of New Jersey certified by the Secretary of State. (*Act Concerning Municipalities, Art. II, Sec. 2, P. L. 1917, p. 320.*)

If the corporate title of the municipality has been shortened, a copy of the resolution shortening the same, as filed in the office of the Secretary of State of New Jersey certified by the Secretary of State. (*Act Concerning Municipalities, Art. III, P. L. 1917, p. 321.*)

3. Certified copies of the ordinances authorizing the improvements for which the bonds are to be issued.

4. A copy of the last annual debt statement of the municipality filed in the office of the Clerk, certified by the Clerk as a true copy of the annual debt statement filed in his office and stating the date of filing. (*Subdiv. 1, Sec. 12, Pierson Bond Act, Chap. 252, P. L. 1916, p. 525, as amended by Chap 108, P. L. 1920, p. 235.*)

5. A copy of the supplemental debt statement of the municipality, made in connection with this issue filed in the office of the Clerk, certified as stated in the preceding paragraph. (*Pierson Bond Act, P. L. 1916, Chap. 252, Sec. 12 (2), p. 525, as amended by Chap. 108, P. L. 1920, p. 235.*)

Although this certificate is all that is necessary for the record of proceedings, it is advisable and customary to prepare and publish a financial statement showing the debts of the municipality in such form that purchasers can tell whether the bonds are legal investments for savings banks.

6. Affidavit or affidavits of the person or persons having knowledge of the facts, stating the position held by such person and that as such he knows the facts, and stating either (a) if the bonds are not assessment bonds, character of the improvement of property and the dates of completion of the improve-

ments and dates of acquisition of the properties for which the bonds are to be issued. (*Pierson Bond Act, Sec. 4 (3), as amended 1917, Chap. 240, p. 804*), or (*b*) if the bonds are assessment bonds, the date when the last installment of assessments will be payable. (*Pierson Bond Act, Sec. 2 (1) (a), as amended 1917, Chap. 240, p. 804.*) This is for the purpose of determining the maturity of the bonds.

7. Extracts, certified by the Clerk, from the Minutes of the meetings of the governing body, at which the said ordinance was introduced and finally passed.

8. An affidavit, or affidavits, made by the manager or publisher of the newspaper or newspapers, in which the ordinance was published prior to final passage. Each of these should state the place where the newspaper is printed, published and circulated, and the date of publication, and should have a clipping attached showing the ordinance as published.

The publication must be at least two days before final passage. After the ordinance should appear the following:

NOTICE.

The (state name of governing body,) of the (state name of municipality,) will consider the final passage of the foregoing ordinance at a meeting to be held on , 19 , at o'clock M., at in the said (city, borough, etc.).

.....

Clerk.

(*Act Concerning Municipalities, Art. X, Sec. 1, as amended by P. L. 1918, p. 479; also Chap. 188, P. L. 1919, p. 418, as amended by P. L. 1921, p. 854.*)

9. An extract, certified by the Clerk, from the minutes of the meeting of the governing body at which the ordinance authorizing the bonds was finally passed.

10. A copy, certified by the Clerk, of the ordinance authorizing the bonds.

11. Affidavits of publication, similar to those described in paragraph 8 showing the publication of the ordinance after final passage.

After the ordinance must appear the words:

Attest:

.....

Clerk.

The following must then follow:

STATEMENT.

The foregoing ordinance was adopted on the day of , 19 .

The bonds authorized thereby will be issued and delivered after the day of , 19 , (specifying a day not less than twenty days after the first publication) and any suit, action or proceeding to set aside or vacate this ordinance must be begun within twenty days after the publication of this statement.

.....

Clerk.

In the case of a borough or township there must be added to the statement:

"Such bonds will not be issued if protests against the same are filed under Section Nine, Chapter 252, P. L. 1916, as amended, unless a proposition for the issuance thereof shall be adopted at an election under said section."

.....

Borough (or township) Clerk.

(*Pierson Bond Act, Sec. 2 (1) (2), as amended 1917, Chap. 240, p. 805.*)

12. A copy, certified by the Clerk, of a certificate made by him and filed in his office showing that there has been no protest against the ordinance, or, in the case of a borough or township, against the issuance of the bonds, and no demand for a referendum. (*Act Concerning Municipalities, Art. XXXVII, Sec. 24, P. L. 1917, p. 461, Walsh Act, Sec. 17, as amended by P. L. 1913, p. 323 and in a borough or township, Pierson Bond Act, Sec. 9, 1916, Chap. 252, p. 534.*) This certificate should not be made and filed until more than ten days after the publication of the ordinance after final passage.

13. An extract, certified by the Clerk, from the minutes of the meeting of the governing body at which the resolution was adopted providing for the form of the bonds and for their sale. (*Pierson Bond Act, Sec. 6, as amended 1920, Chap. 252, p. 469.*) This resolution may be adopted at the time of the final passage of the ordinance authorizing the bonds or at any time thereafter, but the date of sale cannot be within ten days after the publication of the ordinance after final passage.

14. Affidavits of publication, similar to those described in paragraph 8, showing the publication of the notice of sale. The law requires at least ten days' notice of sale published once in the local paper and once in a financial paper published in New York City or Philadelphia. (*Pierson Bond Act, Sec. 6, as amended 1920, Chap. 252, p. 469, and also 1919, Chap. 188, p. 418.*)

15. An extract, certified by the Clerk, from the minutes of the meeting at which the resolution is adopted, awarding the bonds. The minutes should contain a table of the bids received.

The bonds cannot be awarded within ten days after the publication after final passage of the ordinance authorizing the bonds, because such ordinance does not until then become operative. (*Act Concerning Municipalities, Art. XXVII, Sec. 24, Chap. 152, P. L. 1917, p. 261.*)

16. A certificate of the municipal attorney that there is no litigation pending or threatened affecting the bonds. This cannot be made until after the twenty-day period has expired within which litigation can be begun.

After the examination of a record of proceedings containing the proof above described, and such additional proof as may be required in any particular case, a preliminary opinion is given. The bonds can then be taken up and paid for and a final opinion will be given on further proof, consisting of:

17. A certificate by the Treasurer showing the delivery of the bonds and payment for them.

18. A certificate identifying the signatures on the bonds as the signatures of the proper officials, made by an officer of a bank; and

19. An examination of an executed bond.

ADDITIONAL MATTERS.

20. In case any meetings of the governing body are special meetings at which not all the members are present, the record should include proof that each absent member actually received notice of the time, place and object of the meeting. Such proof may be by affidavit of the person who served the notice or by the affidavit of such absent members that they received the notice. The form of notice should be attached. Proof that notice was mailed, without proof that it was received, is not sufficient.

21. All certificates should be dated and those made by the Clerk should have the municipal seal affixed.

22. It is suggested that extracts from the minutes of the governing body be certified by a certificate in substantially the following form:

CLERK'S CERTIFICATE.

I, , Clerk of the (state name of municipality), New Jersey, DO HEREBY CERTIFY that

The annexed extract from the minutes of a meeting of the (state name of governing body) of the (state name of municipality), held on , 19 , has been compared by me with the original and it is a correct transcript therefrom and of the whole of the original so far as the same relates to the matters therein referred to.

This paragraph is for use by a Walsh Act municipality only. (Walsh Act, Sec. 3, P. L. 1912, p. 644.)

The resolution (or ordinance) referred to therein was reduced to writing and read before the vote was taken thereon, and the vote was taken by yeas and nays and entered in the minutes and the minutes of said meeting so recorded were signed by being a majority of all the Commissioners and by the undersigned Clerk.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of said (city, borough, etc.) this day of , 19 .

.....
Clerk.

23. It is suggested that ordinances be certified by a certificate in substantially the following form:

CLERK'S CERTIFICATE.

I, , Clerk of the (state name of municipality), DO HEREBY CERTIFY that

The annexed copy of an ordinance finally adopted at a meeting of the (state name of governing body) of the (state name of municipality), held on , 19 , has been compared by me with the original and it is a correct transcript therefrom and of the whole of the original.

This paragraph is for use by a Walsh Act municipality only. (Walsh Act, Secs. 3 and 6, P. L. 1912, pp. 664 and 649.)

Said ordinance was introduced at a meeting of said Board held on , 19 , and was finally adopted on , 19 . It was complete in the form in which it was finally passed and remained on file with the undersigned clerk for public inspection from the date of introduction, to the date of adoption, being at least two weeks before the final passage or adoption thereof. Said ordinance was recorded and was on , 19 , signed in the book in which it is recorded by the Commissioners whose names appear on the annexed copy, being a majority of all the Commissioners.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of said (city, borough, etc.), this day of , 19 .

.....
Clerk.

24. Extracts from minutes should include the statement of whether the meeting is regular or special, its date, the place where it is held, and the persons present and absent, and the vote for and against each question and the names of those voting aye and nay.

25. The examination of the record of proceedings will be facilitated if, so far as possible, papers are typewritten on standard size legal paper (8 x 13 inches). Sufficient space should be left at the top for binding. Affidavits of publication and other papers of a different size should be attached to standard size paper.

26. Papers referred to in separate numbered paragraphs of this memorandum should not be combined or bound together, in order that they may be arranged in the most convenient order.

Memorandum for Examination of Municipal Bonds

A.

CONSTITUTIONALITY OF ENABLING ACT.

1. Does title express subject of act.
2. Does act embrace more than one subject, if that is prohibited.
3. Is it special legislation, if prohibited.
4. Does it unconstitutionally delegate legislative power.
5. Is it repugnant to other constitutional provisions.
6. *Was it adopted and approved as required by the constitution.
   a. Introduction and separate readings.
   b. Amendments during passage.
   c. Ayes and nays—Required number voting.
   d. Approval by Executive.
   e. Acceptance by municipality.
   f. If act special or local, was notice of application given, if required.

NOTE: *(A) In some states it is necessary to get proof of proper passage and approval. In other states, regularity of passage and approval is conclusively presumed by official promulgation.

(B) If statute is contained in *legislative revision,* it may be relied upon; but if in mere *codification* or *compilation,* original session laws must be examined.

B.

DEBT LIMITATIONS.

7. Are there any constitutional or general statutory limitations of indebtedness; if so, has the margin of debt-incurring capacity been exceeded.
   a. Total debt, including this issue.
   b. Deductions which may be made to ascertain net debt.
   c. If necessary, include debt of other municipalities covering in whole or in part same territory.
   d. What is assessed valuation, or population, or other facts upon which limitations depend.

NOTE: In New York see that assessed valuation of cities is *as equalized by County Board.*

C.

INCORPORATION.

8. Is municipality duly incorporated.
   a. By special act.
   b. By proceedings under general act.
   c. Have general governmental referendum acts been accepted.
   d. Is there a time limit on corporate existence.

D.

POWER TO ISSUE.

9. Does act relied upon confer authority to issue bonds as proposed.

10. Does act confer power to issue bonds for particular purpose or only generally for any municipal purpose; if latter, is purpose specifically provided for in any act or necessarily implied.

11. Does it confer power to issue bonds of the maturities and interest rate proposed.

12. Does it contain any limitation as to amount, either fixed or percentage of assessed valuation, or amount per capita or otherwise, or amount which may be issued in any year.

13. Will bonds be general obligations of municipality.

14. Does act contain adequate taxing power, or are there tax limitations which affect the principal or interest of bonds.

15. Are bonds limited to actual cost or expense; if so what may be included in cost or expense.

E.

ACTION BY ELECTORS.

If authorization by voters required:

16. Has all action required of bodies or officers preliminary to and directing the election been taken.
    a. Is action required to be by resolution or ordinance.
    b. Was action taken at regular, stated, or special meetings.
    c. If special, was meeting duly called.
    d. Was a quorum present.
    e. Introduction, readings and passage at separate meetings.
    f. Did required number vote.
    g. Approval by Mayor or Chief Executive, or passage over veto.
    h. Was ordinance or resolution recorded, if required.
    i. Was ordinance or resolution published, if required.
    j. Was any protest filed which would prevent calling election.

17. Is form of notice of election proper, and does it conform to preliminary proceedings.
    a. Statement of purpose of appropriation or bonds, and any details as to purpose or terms of bonds.
    b. Date of election.
    c. Place or places.
    d. Description of election districts, if required.
    e. Hours.
    f. Qualification of voters.
    g. Signed by proper officers.

18. Was it posted and published, if both are required, in requisite manner, and for requisite periods and times. Were newspapers official if required.

19. Regularity of registration of voters, if necessary to be inquired into.

20. Was ballot, and proposition thereon, sufficient in form and substance.
    a. Did the proposition fully state the matters required to be voted upon in accordance with statute and preliminary proceedings.
    b. Did it combine two or more purposes, if prohibited.
    c. Was it official if required.

21. Was the canvass of the result of the election properly made, and was the result of the election determined by the required officer or body, and does the result of the election show the requisite affirmative vote.

F.

ACTION BY GOVERNING BODY.

22. Are all proceedings subsequent to vote, or, where no vote is required, all proceedings of bodies or officers duly adopted and proper in form and substance.
    a. Is a resolution or ordinance required.
    b. Was each ordinance or resolution properly introduced, read required times, and finally passed, on separate days, and at stated or regular meetings, if required, or, if at special meeting, was it duly called.
    c. Was quorum present at each step and was requisite vote obtained at each step by ayes and nays if required.*

d. Was ordinance or resolution approved by Executive or passed over veto.
e. Was it recorded.
f. Was it duly published.
g. Was it duly posted.

23. Was resolution or ordinance in proper form as to title and enacting clause.

24. Does authorizing ordinance or resolution contain complete authority for, and details as to purpose and bonds, conforming to the statute and previous proceedings, including proper tax or sinking fund provision.*

25. Has form of bond been adopted.

* NOTE: General Municipal Law, New York, Sec. 5, requires two-thirds vote and statement of purpose and provision for taxes to pay principal and interest.

G.

CONSENTS OF OTHER BOARDS OR BODIES.

26. Have all consents or action by Boards, other than authorizing body, been obtained, such as State Boards in New York as to water, sewerage, lighting, etc.; Congress or Secretary of War as to bridges over navigable streams.

H.

SALE.

27. If public sale required.
a. Has proper notice, by publication or posting, been given, and does offering conform to previous proceedings.
b. Was notice given pursuant to proper direction.
c. Was it necessary to offer bonds first to any sinking fund or other board.

I.

AWARD.

28. Have bonds been duly awarded by the proper authority.
a. Does bid conform to notice of sale, if any required or given, at more than par and interest or if at less than par is this permissible.
b. To highest bidder, or person bidding lowest rate, if required.

J.

PAYMENT.

29. Were bonds properly paid for.
a. Did municipality receive par, premium and accrued interest.

K.

FORM OF PROOF.

30. Are proofs in proper form.
    a. Are all records properly certified.
    b. Are all affidavits in proper form.
    c. Are officials making certificates or affidavits proper officers having charge of records or peculiar knowledge of facts.
    d. Are records properly certified.
    e. Are affidavits of publication originals, and do they show exact dates of publication, with clipping attached.

L.

FORM OF BOND.

31. Is form of bond correct.
    a. Proper designation of bond, when statute provides therefor.
    b. Proper name of obligor.
    c. Proper name of obligee, if registered.
    d. Date.
    e. Dates of maturity.
    f. Principal amount.
    g. Principal where payable.
    h. Interest rate.
    i. Dates of payment of interest.
    j. Interest where payable.
    k. Medium in which principal and interest payable.
    l. Correct recital of authorizing resolution and vote of electors if required.
    m. Correct recital of statutory authority.
    n. Correct statutory form of recital giving conclusive presumption of legality, if authorized.
    o. General recital.
    p. Signed by proper officers.
    q. Sealed with proper seal.
    r. Were officers signing in office at time of actual delivery and payment.
    s. Are provisions for registration and transfer, conversion or exchange, proper, including endorsement.
    t. If coupon, is the form and amount of the coupon correct, and properly authenticated.

M.

MISCELLANEOUS.

32. Do proofs show election and qualification, of all officers acting in the authorization and issuance of the bonds (especially those signing).

33. Where referendum act is relied upon for authority or procedure, get complete proof of acceptance.

34. Where statute permits referendum on acts of municipal bodies, or permits recall or officers see that no referendum or recall was had; or, if any, the result.

35. Where any proceeding in connection with the bonds is to be initiated by petition, is petition adequately signed; if by owners of real estate eliminate executors, and if necessary get special proof as to corporations, trustees, partners and cases other than individuals.

36. If statutes prohibit elections within particular periods or within period after previous election, see that vote was not within such period, as in N. Y. Village Law or Penn. Genl. Indebtedness Statute.

37. In New York cities proof that certificate has been filed under Home Rule Law (L. 1913, ch. 247).

N.

LITIGATION.

38. Have bonds been judicially passed upon or is any litigation pending or threatened.

O.

39. REFUNDING BONDS.

a. Was issue to be refunded, legally issued if that must be investigated.
b. Are bonds to be refunded outstanding and are there funds applicable to their payment.
c. Were old bonds duly paid for.
d. Has there been any litigation on old bonds.
e. Where statutes restrict refunding to bonds not declared invalid, official court searches must be secured.
f. Can proceeds exceed principal or fixed proportion of old bonds.

P.

FUNDING BONDS.

40. Can they be issued to realize more than principal of existing debt or any part thereof.

Chapter XVIII

PRACTICAL SUGGESTIONS

The rules of the game.—The municipal bond game is an extremely interesting pastime. Like bridge-whist or poker, the latter of which to some extent it resembles, it is played according to a number of rules, most of which are prescribed by higher authority, but a few are made by the players themselves. Certain consequences follow from the application of these rules. Custom decides how certain things shall be done, and experience shows that if the rules are followed, better results are obtained than if the rules, or some of them, are ignored. It is the purpose of this concluding chapter to draw deductions from experience and state the deductions as suggestions to municipal officials.

Publicity.—Advertise your bonds for sale in the financial newspapers which circulate in the locality from which you expect bids. There are no better mediums for general purposes than the *Daily Bond Buyer* and the *Commercial and Financial Chronicle* of New York. Both of these papers reach every bond house of consequence in the United States. If you give your proposed sale sufficient publicity, you will, certainly in normal times and probably in most times, have no difficulty in securing bids which you can accept. Do not rely upon advertising in local newspapers which do not reach the bond dealers, or connive to shut out bids by doing the least permissible amount of advertising.

The following is a list of financial publications and the territories in which they circulate. This list is not intended to be inclusive, but it is believed that it is representative.

The Bond Buyer (New York, N. Y.)

This publication (issued daily and weekly) is the technical organ of the municipal bond business, being devoted exclusively to this one class of securities. It is the paper usually selected by municipalities in which to publish bond sale notices, bond calls, etc. Municipal bond dealers, banks operat-

ing bond departments and important investors in municipal issues depend mainly upon the *Bond Buyer* for information relating to new State, city and other municipal bond issues. Circulation is national.

The Commercial and Financial Chronicle (New York, N. Y.)

The *Chronicle* is the standard weekly financial journal of the United States and is found in the offices of bankers, brokers and financial institutions, and is quite widely read by investors. It has a "State and City Department" in which is published news of current municipal finance. Circulation is national.

The Wall Street Journal (New York, N. Y.)

This is the leading financial daily, and enjoys a wide circulation among bankers, brokers, investors, etc. Banking and corporation news and the stock, bond and money markets are carefully covered. Circulation is national.

Boston News Bureau (Boston, Mass.)

In New England, the *Boston News Bureau* virtually duplicates the *Wall Street Journal.* These two publications are closely allied.

The Manufacturers Record (Baltimore, Md.)

This paper is the leading trade journal of the South. Departments are devoted to construction and financial news, in which considerable attention is given to public improvement work and public finance. Carries a considerable number of official notices of Southern municipal bond offerings. Circulation is national.

The Economist (Chicago, Ill.)

The leading financial weekly of the Middle West. Devoted to general financial and real estate news. Local circulation.

The Commercial West (Minneapolis, Minn.)

Financial weekly of the twin cities district. Devotes about a page to municipal finance in its own district. Carries some local municipal bond advertising.

The Coast Banker (San Francisco, Cal.)

Leading banking and financial paper of the Pacific Coast. Circulation local. Issued monthly.

Pacific Banker (Portland, Ore.)

A banking and investment weekly covering Oregon, Washington, and vicinity. Reaches local municipal bond dealers.

Another means of advertising.—United States Mortgage and Trust Company of New York City offers a very valuable service for a reasonable charge. It will prepare and mail to a selected list of dealers a circular describing the bonds offered for sale, together with a financial statement (prepared from information furnished by the municipal officials), and form for bids or proposals.

Preparation of bonds.—The necessary precautions against forgery and fraud which should surround the issuance of municipal securities, have not always been exercised. Cheaply printed blanks of poor quality are frequently used and the preparation is not subject to the expert supervision under which all bonds should be issued.

The possibility of forgery.—The first of the year 1919 brought to light the methods by which M. H. Cutter of Chicago had forged bonds of a half dozen cities and towns, the issues involved amounting to about $600,000. His own firm bought and attended to the engraving of the bonds, thus removing the check against overissue and enabling Cutter to forge the bogus bonds and manipulate all of the various issues at will. The serious losses resulting recalled the Quigley and Prior forgeries of preceding decades.

The lack of precaution on the part of many municipalities in the issuance of their securities is disquieting, especially when it is considered that such obligations form a substantial part of the investments of executors, trustees, insurance companies, and banks. For a municipality to sacrifice the necessary safeguards in the issuance of securities by any reduction in expense and thereby diminish the actual value of the security to the dealer and to the investor, is to obtain their preparation at a correspondingly high cost of risk.

How fraud may be avoided.—Have your bonds printed and prepared by a responsible banknote company, and deal direct with the printers. The preparation of coupon bonds requires a high degree of skill and experience, both being necessary if annoying and costly mistakes are to be avoided. The financial newspapers will furnish names and addresses of the banknote companies, which alone are competent to do such work.

United States Mortgage and Trust Company, the depositary of the Investment Bankers Association, will prepare bonds on its own specially water-marked paper, attend to the execution of the bonds, and guarantee the genuineness of the signatures of the municipal officials and the seal impressed thereon, at prices only slightly above those for which the same bonds could be secured elsewhere. A similar service is offered by Security Bank Note Company of Philadelphia and Chemical Bank Note Company of Rutherford, New Jersey. Bonds so prepared and certified are somewhat more attractive to dealers than bonds not so prepared and certified, and probably bring a better price.

Contracts for the preparation of bonds made with other than banknote companies may be unduly expensive because an agent's profit is included in the price. Even if you are offered a contract calling for the payment of $500 for the preparation of a small issue of bonds, do not sign it. In one instance which came to the writer's attention, a contract of this kind was made and broken when it was found that the bonds could be prepared for $80.

Side agreements.—It is inadvisable to make private contracts for the sale of bonds, or to enter into deposit, fiscal agent or proceedings contracts, for the reasons which appear in Chapter IX. It is ordinarily unnecessary to make contracts of this kind, and it is in connection with such contracts that unpleasant incidents arise.

In dealing with bond houses and bond men, it should be borne in mind that the representatives of the better class of bond houses are very highly trained men. These men are ethical and fair in their dealings with municipal officials, but the municipal official is at a disadvantage in dealing with them. The American theory of government is that any person elected to public office is fully competent to perform the duties of that office. As a matter of fact, the average municipal official is not a match for the skilled bond buyer.

Place of payment.—It is an advantage to the municipality to contract to pay interest and principal of bonds at a New York bank or a par point, that is, a city in which the banks are not charged with exchange for the collection of checks. Local banks like the business and the advertising which follow the deposit of funds in advance of and to meet such payments, and the naming of the bank in the bond and coupons

as the designated place of payment. But bonds payable in New York or at a par point bring a better price.

Promptness in payment.—Have funds on hand in the designated bank for the payment of interest and principal before either are due. This will preserve your credit and save you a great deal of annoyance. It may seem a small thing to delay for a few days the payment of semi-annual interest coupons, but it is a cause of alarm to your bondholder. If coupons are presented and no funds are available, they will be returned through the usual channels to the bank with which deposited, and by that bank to the depositor. Even if the depositor is subsequently advised that the coupons will be paid, the process of collection must be again put into motion.

Employment of counsel.—When a bond issue is contemplated, it should be remembered that sooner or later the proceedings will be passed upon by counsel generally recognized to be specialists in the examination of such proceedings.

Until recent years, it was the practice for the purchaser to select his own attorney, but within the last decade the practice has become well established, at least in the Eastern States, for the municipality to retain expert counsel in the first instance and have him conduct all of the proceedings in connection with the bond issue, and give his final approving opinion when the bonds are delivered. This does not imply any reflection upon the city's own counsel. The smaller municipality issues bonds at infrequent intervals, and political changes are sufficiently rapid so that the corporation counsel may have occasion to conduct no proceedings for the issue of bonds. The specialists are willing to work with local counsel, and in fact prefer doing so. If the city retains the expert, it is of course responsible for his fee, but the amount of the fee is included in the higher price received for the bonds when sold. If the bidder knows that he must retain his own attorney, he will make an allowance for the fee in submitting his bid. If he does not have to meet this item of expense, his bid will be higher.

Modern practice requires the municipality to furnish an acceptable, that is a merchantable, legal opinion with its bonds, and dealers understand that their money, time, and effort will not be wasted and the bonds will be promptly delivered, if such an opinion is forthcoming.

APPENDICES

Appendix A

OUTLINE ANALYSIS OF SUBJECT

Chapter I

THE PROBLEM STATED

A. The municipal bond is a creature of law.
   a. General principles must be studied.
B. The municipality existed before the nation.
C. Municipal needs create municipal debt.
D. Necessity for borrowing money.
   a. Annual taxation inadequate; illustrated.
E. Procedure of bond issue outlined.
F. Forms of:
   a. Tax ordinance;
   b. Municipal budget;
   c. Bond ordinance.

Chapter II

THE MUNICIPAL BOND

A. Is a negotiable instrument:
   a. Attributes of negotiability;
   b. Municipal bond has all these elements;
   c. Loses for the time its negotiability by delivery, if registered.
B. Conditions of negotiability.
C. The component parts of a municipal bond are:
   a. Face:
      1. Title of the instrument;
      2. Form:
         (1) Name of promissor;
         (2) Name of promisee;
         (3) Principal sum to be paid;
         (4) Due date; a promise to pay;
         (5) Interest at the rate stated;
         (6) The place and medium of payment;
         (7) Conversion provision;
         (8) Recital of authority and purpose;
         (9) Estoppel clause;
         (10) Testimonium;
         (11) Signatures and seal.
   b. Coupon, which is an independent promise to pay.
   c. Back:
      1. Filing.
      2. Panels upon which appear forms for the registration certificates.

Chapter III

MUNICIPAL CORPORATIONS

A. a. Definition of municipal corporations.
   b. They are creatures of the State.
      1. Constitutional provisions, and
      2. Legislative control.
   c. They are created by:
      1. Special charter or pursuant to
      2. General laws, and may be
      3. De facto corporations.

B. a. Powers of municipal corporations are
      1. Express, the principal powers being the
         (1) Police power;
         (2) Power of taxation, and
         (3) Eminent domain.
      2. Implied, incident to the express grant.
   b. Powers of municipal corporations are divided into
      1. Governmental, and
      2. Proprietary powers.

C. a. Municipal corporations are classified as
      1. Counties;
      2. True municipal corporations, and
      3. Quasi-municipal corporations, among which are
         (1) School districts and various
         (2) Taxing districts.

Chapter IV

MUNICIPAL PROPERTY AND IMPROVEMENTS

A. Increase of public activities.
   a. Earliest recorded history shows co-operation in construction of:
      1. Roads;
      2. Bridges;
      3. City walls.
   b. Public health was seen to require:
      1. Water;
      2. Sewers;
      3. Baths.
   c. Public charity and the humanizing influence of Christianity created:
      1. Hospitals;
      2. Asylums.
   d. The evolution of the modern city.

B. Municipal expenditures.
   a. General considerations; what is a municipal purpose?
   b. The expenditures are for:
      1. Running expenses;
      2. Debt service, funds for which are raised by annual taxation, and
      3. Public property or improvements, funds for which are borrowed.

c. Improvements are made and property is acquired in one of two capacities:
   1. Governmental and
   2. Proprietary.

C. Public Property.
   a. Capacity to hold and acquire property.
   b. Mode of acquisition is by
      1. Purchase;
      2. Gift;
      3. Condemnation.
   c. Limitations on acquisition are:
      1. Popular vote and the
      2. Referendum.

D. Public Improvements.
   a. Nature and grounds of power to make.
   b. Statutory provisions such as:
      1. Act Concerning Municipalities in New Jersey;
      2. Second-Class Cities Law and the Village Law in New York.
   c. Are, among others:
      1. Public buildings;
      2. Streets, ways and bridges;
      3. Sewers and drains;
      4. Water supply;
      5. Lighting;
      6. Wharves and docks;
      7. Parks and public places;
      8. Markets;
      9. Schools;
      10. Libraries.

E. Improvements outside of municipality.
F. Public utilities.
G. Building houses and selling commodities to public.

Chapter V

TAXATION AND LIMITATION OF TAXES

A. The Power to Tax.
   a. Tax defined.
   b. Primary form a direct property tax.
   c. Power to tax is
      1. Inherent in the sovereign;
      2. Exercised by the legislature which may delegate it to
         (1) Municipalities, and to
         (2) Local boards.
   d. Taxes can be levied only for public use.

B. Classes of taxes defined.
   a. Capitation or poll.
   b. Property.
      1. General.
      2. Assessments.
   c. Excise and income.

C. Taxation for debt service.
   a. Illustrated.
   b. Its importance.

D. Limitations on tax rates.
   a. Illustrated.
   b. Arguments against any tax limit for general purposes.
   c. Arguments against any tax limit for debt service.
E. Revenues.

Chapter VI

MUNICIPAL BORROWING

A. The power to incur indebtedness.
   a. Nature and scope.
   b. Municipal purposes.
   c. Does not include the power to issue negotiable securities.
B. Limitations on the power to incur debt.
   a. General considerations.
   b. Limitations are
      1. Constitutional or
      2. Statutory.
   c. Illustrated.
C. The power to issue negotiable instruments.
   a. Original issues.
      1. Nature of power.
      2. Nature of power is wholly statutory.
   b. Illustrated.
   c. Refunding.
   d. Ratification by legislature.
D. Short-term loans.

Chapter VII

THE PROMISSOR IN THE BOND

A. The Sovereign or the State.
   a. Cannot be sued without its consent.
B. The county.
   a. The same property is taxed which is taxed for municipal purposes.
   b. Debt of subdivisions.
   c. Debt small compared to assessed valuation.
C. The municipality, which may have:
   a. Implied power to borrow but must have
   b. Express power to issue negotiable instruments.
D. The quasi-municipality, which may
   a. Borrow and tax;
   b. Borrow but not tax;
   c. Be taxed but may not borrow.

Chapter VIII

THE PROMISE AND THE PURPOSE OF THE BOND

A. The character of the promise.
   a. Limited by tax rates:
      1. Constitutional.
      2. Statutory.
      3. Results in limited obligation.

b. Limited to a special fund, i.e., assessments.
   1. Bonds may not be negotiable instruments.
   2. Federal tort theory.
c. Limited by area of land taxed.

B. The purpose.
   a. Bonds issued for self-sustaining public utilities such as:
      1. Water works.
      2. Wharves, docks and markets.
   b. Bonds issued for non-revenue producing improvements such as:
      1. Streets and sewers.
      2. Schools, hospitals and parks.

Chapter IX

THE MATURITY OF THE BOND

A. Bonds may be classified as to time of payment:
   a. Term bonds which are absolutely
      1. Due and payable at one time, or
      2. Callable after a stated date.
   b. Debt service for term bonds: sinking funds.
      1. Contract with bondholder;
      2. Disadvantages of sinking funds.
   c. Serial bonds which are payable in:
      1. Equal annual installments;
      2. Substantially equal annual installments;
      3. Deferred installments.
   d. Debt service for serial bonds: no sinking fund.

B. Term of bonds may be limited to life of improvement.
   a. Reason for such limitation.

Chapter X

SALE AND AWARD

A. Private Sale defined.
   a. Advantages:
      1. To municipality;
      2. To broker.
   b. Disadvantages:
      1. To municipality;
      2. To broker.

B. Public Sale defined.
   a. Advantages to municipality:
      1. Competition;
      2. Protection to officers.
   b. Disadvantages to municipality:
      1. Market conditions;
      2. Technical errors in procedure.
   c. Illustrative statutory provisions:
      1. In New York;
      2. In New Jersey.

C. Par Sales are required by most statutes.
   a. Economic fallacy.
   b. Political necessity.
   c. Evasion by

1. Fiscal agency contracts;
2. Proceedings contracts;
3. Deposit agreements.
d. Expenses of sale.
e. Irregularities in procedure.
D. Brokerage and commissions.
E. Forms of
a. Notice of sale;
b. Propositions pursuant thereto.

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DEFAULT, AND REMEDY OF THE BONDHOLDER

A. Default defined.
a. Consequences as to:
1. Interest;
2. Principal.
b. Prevalence of.
c. Reasons for.
1. Inability, because of
(1) Lack of authority to issue;
(2) Limited tax rate;
(3) Shrinkage of assessed valuations.
2. Bad faith.
B. Remedy of the Bondholder.
a. Bonds are not liens upon specific property.
b. Necessity for obtaining judgment.
c. Mandamus to levy tax.
1. Where sufficient tax may be levied.
2. Where sufficient tax may not be levied.
d. Actions based on contract.
e. Legislative relief.
f. Good faith of issuing municipality.

Chapter XII

BONDS AS INVESTMENTS

A. Definition and general considerations.
B. Investments by individuals.
a. Elements of an ideal investment:
1. Security of principal;
2. Fixed or definite interest;
3. Fair income return;
4. Merchantability;
5. Good collateral for loans;
6. Freedom from taxation;
7. Freedom from care;
8. Satisfactory maturity;
9. Convenient denomination;
10. Possibility of appreciation.
B. Investments by fiduciaries.
a. Executors, trustees and savings banks.
1. Regulated by statutes—Illustration.
C. To secure postal savings deposits.

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TAXATION OF BONDS

A. General considerations.
B. The taxing power.
   a. Definition of the taxing power.
   b. Taxing power of the United States.
   c. Limitations upon the Federal taxing power.
   d. Taxing power of the States.
   e. Limitations upon the taxing power of the States.
C. Taxation of the principal of State and municipal bonds.
   a. Taxation by the United States.
   b. Taxation by the States.
D. Taxation of the income of State and municipal bonds.
   a. Nature of the tax.
   b. Taxation by the United States; the 16th amendment to the Federal Constitution.
   c. Taxation by the States.
E. Taxation of bonds of non-residents.
F. Inheritance Taxes.

Chapter XIV

VALUATION OF BONDS

A. Money is a commodity. The price of its use is:
   a. Interest:
      1. Normal yield.
      2. Net yield.
      3. Tables of bond values.
      4. Basis.
   b. Fluctuations and differences in yield.
   c. Purchasing power of money.
   d. Market conditions.
B. Bonds are not equally valuable; differences exist between bonds of
   a. City;
   b. County;
   c. Tax districts, etc.
C. Bonds of the same class are not equally valuable. The factors are:
   a. Valuations of taxable property;
   b. Indebtedness;
   c. Tax rates;
   d. Population;
   e. Municipal credit.
D. The practice of valuation described.
E. Differences in expert opinion.
F. Sources of information.

Chapter XV

INCONTESTABILITY AND VALIDATION

A. The menace of default.
   a. Improvement in standards of honesty.
   b. Improvement in legislation.

B. Estoppel by recital.
  a. Defined.
  b. Effect.
C. Short statutes of limitations.
  a. Illustrations.
D. Validation by decree of
  a. Administrative department;
  b. Court.
    1. Doctrine of *res adjudicata.*
    2. Constitutional difficulties illustrated.
  c. Court in Georgia.
E. Registration by officials, effect when
  a. Judicial function;
  b. Ministerial function.
F. Certification of signatures and seal.

Chapter XVI

PARTICULAR BONDS

A. Considered as to issuing unit:
  a. Cities;
  b. Counties;
  c. Minor municipalities;
  d. Tax districts.
B. Considered as to purpose:
  a. To provide income-producing utilities;
  b. To provide other properties or improvements.
C. Considered as to payment:
  a. Payable from direct general tax;
  b. Payable from assessments.
D. Considered as to popular assent:
  a. Electoral bonds.

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THE ATTORNEYS' FUNCTIONS

A. General considerations.
  a. Difficulties usually arise before issue.
B. When retained by the municipality.
  a. The advantages.
  b. The procedure.
C. When retained by the purchaser.
  a. The disadvantages.
  b. The procedure.
  c. Failure to approve.
D. The record of proceedings.
  a. Enables counsel to form opinion.
  b. Contents of the record.
E. The opinion.
  a. Its usual form, preliminary and final.
  b. The meaning of the opinion.
  c. Qualified opinions.
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PRACTICAL SUGGESTIONS

A. Publicity of bond sales.
   1. Advertising. List of periodicals.
   2. Circulars.
B. Preparation of bonds—certification.
C. Side agreements with dealers.
D. Place of payment of principal and interest.
E. Promptness in payment.
F. Employment of counsel.

Appendix B

THE MUNICIPAL FINANCE ACT OF NORTH CAROLINA.

An Act to Amend and Re-enact the Municipal Finance Act, Being Sections 2918 to 2961, Consolidated Statutes of North Carolina.

The General Assembly of North Carolina do enact:

Section 1. That sections two thousand nine hundred and eighteen to two thousand nine hundred and sixty-nine, inclusive, of the Consolidated Statutes of North Carolina be and are hereby amended and reënacted to read as follows: Sections of law amended and reënacted.

SUBCHAPTER III. MUNICIPAL FINANCE ACT

Article 23. General Provisions

2918. *Short title.* This act may be cited as "The Municipal Finance Act, 1921." Short title.

2919. *Meaning of terms.* In this act, unless the context otherwise requires, the expressions: Terms defined.

"Bond ordinance" means an ordinance authorizing the issuance of bonds of a municipality; Bond ordinance.

"Clerk" means the person occupying the position of clerk or secretary of a municipality; Clerk.

"Financial officer" means the chief financial officer of a municipality; Financial officer.

"Funding bonds" means bonds issued to pay or extend the time of payment of debts incurred before December sixth, one thousand nine hundred and twenty-one, not evidenced by bonds; Funding bonds

"Governing body" means the board or body in which the general legislative powers of a municipality are vested; Governing body.

"Local improvement" means any improvements or property the cost of which has been or is to be specially assessed in whole or in part; Local improvement.

"Municipality" means and includes any city, town, or incorporated village in this State, now or hereafter incorporated; Municipality.

"Necessary expenses" means the necessary expenses referred to in section seven of article seven of the Constitution of North Carolina; Necessary expense.

"Publication" includes posting in cases where posting is authorized by this act as a substitute for publication in a newspaper; Publication.

"Refunding bonds" means bonds issued to pay or extend the time of payment of debts incurred before March seventh, one thousand nine hundred and seventeen, evidenced by bonds; Refunding bonds.

Special assessments.

"Special assessments" means special assessments for local improvements, levied on abutting property or other property specially benefited, or on street railroad companies or other companies or individuals having tracks in streets or highways, and "specially assessed" has a corresponding meaning.

Specially assessed.

Publication of ordinances and notices.

2920. *Publication of ordinance and notices.* An ordinance or notice required by this act to be published by a municipality shall be published in a newspaper published in the municipality, or, if no newspaper is published therein, in a newspaper published in the county and circulating in the municipality, or, if there is no such newspaper, the ordinance or notice shall be posted at the door of the building in which the governing body usually holds its meetings and at three other public places in the municipality.

Application and construction of act.

2921. *Application and construction of act.* This act shall apply to all municipalities. Every provision of this act shall be construed as being qualified by constitutional provisions, whenever such construction shall be necessary in order to sustain the constitutionality of any portion of this act. If any portion of this act shall be declared unconstitutional, the remainder shall stand, and the portion declared unconstitutional shall be exscinded.

Article 24. Budget and Appropriations

Fiscal year.

2922. *The fiscal year.* The fiscal year of every municipality shall begin either on the first day of June or on the first day of September, as the governing body of the municipality may determine.

Preparation of budget.

2923. *Budget prepared.* Not earlier than one month before, nor later than one month after the beginning of each fiscal year of a municipality, the governing body shall cause to be prepared a plan for financing the municipality during said fiscal year, which plan shall be known as the budget and shall be based upon detailed estimates furnished by the several departments and other divisions of the municipal government.

Basis of budget.

Contents of budget.

2924. *What budget shall contain.* The budget shall present the following information:

Itemized estimate of expenses.

1. An itemized estimate of the appropriations necessary to be made for the current expenses and for permanent improvements for each department and division of the municipal government for the fiscal year (exclusive of expense to be paid for by means of bonds issued under article twenty-six of this chapter), for the payment of the principal and interest of debts and for deficits of the previous fiscal year, with comparative statements in parallel columns of expenditures for corresponding items so far as possible for the two preceding fiscal years. This estimate may include a contingent fund not designated for any particular purpose not exceeding five per centum of the total estimated amount of other appropriations.

Contingent fund.

Itemized estimate of taxes and revenue.

2. An itemized estimate of the taxes required and of the estimated revenues of the municipality from all other sources for the fiscal year, the unencumbered balances of the appropriations, and of the surplus revenues of the previous fiscal year, with comparative statements in parallel columns of the taxes and other revenues for the two preceding fiscal years.

3. A statement of the financial condition of the municipality, and such other information as the governing body may deem advisable to state. Statement of financial condition. Other information.

2925. *Copy of budget filed for inspection.* A copy of the budget shall be filed in the office of the clerk of the municipality for public inspection not later than ten days before its adoption by the governing body, and a public hearing shall be given thereon by the governing body before the adoption of the budget, notice of which hearing shall be published. Copy of budget filed. Public hearing.

2926. *Change of fiscal year.* The fiscal year may be changed by resolution of the governing body, which resolution shall declare that the fiscal year shall thereafter begin on the first day of September or June, as the case may be. A budget and appropriation ordinance shall be adopted for a period commencing at the expiration of the current fiscal year, in which such resolution is passed, and ending at the end of the next succeeding new fiscal year. Such a budget shall be adopted within the month preceding or the month following the beginning of such period. Fiscal year may be changed. Budget and appropriation ordinance. Time for adoption of budget.

2927. *Annual appropriation ordinance.* Not later than one month after the beginning of the fiscal year, the governing body shall pass the annual appropriation ordinance for the fiscal year, which shall be based on the budget. The total amount of appropriations shall not exceed the total of the estimated revenue, unencumbered balances and surplus receipts. Annual appropriation ordinance. Limit of appropriations.

2928. *Appropriations made before annual ordinance.* In the interval between the beginning of a fiscal year and the adoption of the annual appropriation ordinance the governing body may make appropriations for the purpose of paying fixed salaries, the principal and interest of bonded debts and other loans, the stated compensation of officers and employees and indebtedness for work performed or materials furnished under contracts made before the beginning of the fiscal year, or for the ordinary expenses of the municipality, which appropriations shall be chargeable to the appropriations in the annual appropriation ordinances for that year. Temporary appropriations. Purposes.

2929. *Amendment of appropriations.* At any time after the passage of the annual appropriation ordinance, the governing body may amend such ordinance so as to authorize the transfer of balances appropriated for one purpose to another purpose, or to appropriate available revenues not included in the annual budget. Amendment of appropriations.

The amendatory ordinance, unless it be for the appropriation of available revenues not included in the annual budget, shall be published one or more times at least one week before its final passage, with notice of the time when and place where it will be finally passed: *Provided, however,* that such ordinance may be passed during the last three months of a fiscal year, without any previous publication or notice. Amendatory ordinance to be published. Proviso: Amendment within last quarter.

2930. *Balances revert for future appropriations.* At the close of each fiscal year the unencumbered balance of each appropriation shall revert to the general fund, and shall be subject to future appropriation. Balances subject to future appropriations.

2931. *Funds specially applied not affected.* Nothing herein shall be construed to permit revenues which by statute are appropriated to a particular purpose to be appropriated to any other purpose, but such revenue shall nevertheless be included in the budget. Funds appropriated by statutes.

ARTICLE 25. TEMPORARY LOANS

Temporary loans in anticipation of collections.

2932. *Money borrowed to meet appropriations.* A municipality may borrow money for the purpose of meeting appropriations made for the current fiscal year, in anticipation of the collection of the taxes and revenues of such fiscal year, and within the amount of such appropriations. Such loans shall be paid not later than the tenth day of October in the next succeeding fiscal year. Provision shall be made in the annual budget and annual appropriation ordinance of each fiscal year for the payment of all unpaid loans predicated upon the taxes and revenues of the previous fiscal year.

Payment of loans.

Budget to provide for payment of loans.

Loans to pay judgments or interest.

2933. *Money borrowed to pay judgments or interest.* For the purpose of paying a judgment recovered against a municipality, or paying the principal or interest of bonds due or to become due within two months and not otherwise adequately provided for, a municipality may borrow money in anticipation of the receipt of either the revenues of the fiscal year in which the money is borrowed or the revenues of the next succeeding fiscal year. Such loans shall be paid not later than the end of such next succeeding fiscal year. In the event, however, that a judgment or judgments against a municipality amount to more than one cent per hundred dollars of the assessed valuation of taxable property of the municipality for the year in which taxes were last levied before the recovery of the judgment, a loan to pay the judgment may be made payable in not more than five substantially equal annual installments, beginning within one year after the loan is made.

Time for payment.

Loans exceeding one per cent of tax values.

Loans in anticipation of bond sales.

2934. *Money borrowed in anticipation of bond sales.* At any time after a bond ordinance has taken effect as provided in article twenty-six herein, a municipality may borrow money for the purposes for which the bonds are to be issued, in anticipation of the receipt of the proceeds of the sale of the bonds, and within the maximum authorized amount of the bond issue. Such loans shall be paid not later than three years after the time of taking effect of the ordinance authorizing the bonds upon which they are predicated. The governing body may, in its discretion, retire any such loans by means of current revenues, special assessments, or other funds, in lieu of retiring them by means of bonds: *Provided, however,* that the governing body, before the actual retirement of any such loan by any means other than the issuance of bonds, under the bond ordinance upon which such loan is predicated, shall amend or repeal such ordinance so as to reduce the authorized amount of the bond issue by the amount of the loan to be so retired. Such an amendatory or repealing ordinance shall take effect upon its passage and need not be published.

Maximum amount.

Time of payment.

Power to retire loans.

Proviso: Reduction of bond issue.

Negotiable notes.

2935. *Notes issued for temporary loans.* Negotiable notes shall be issued for all moneys borrowed under the last two sections. Such notes may be renewed from time to time and money may be borrowed upon notes from time to time for the payment of any indebtedness evidenced thereby, but all such notes shall mature within the time limited by said sections for the payment of the original loan. No money shall be borrowed under said sections at a rate of interest exceeding the maximum rate permitted by law. The said notes may be disposed of by public or private negotiations. The issuance of such notes shall be authorized by resolution of the governing body, which shall fix the actual or maximum face amount of the notes and the actual or maximum rate of

Renewal.

Final limit.

Interest rate.

Sale of notes.

Resolution for temporary loans.

interest to be paid upon the amount borrowed. The governing body may delegate to any officer the power to fix said face amount, and rate of interest within the limitations prescribed by said resolution, and the power to dispose of said notes. All such notes shall be executed in the manner provided in section two thousand nine hundred and fifty-four of this subchapter in relation to bonds. They shall be submitted to and approved by the attorney for the municipality before they are issued, and his written approval indorsed on the notes.

Delegation of powers.

Execution of notes.

Approval of attorney.

Article 26. Permanent Financing

Permanent financing.

2936. *Not applied to temporary loans.* The provisions of this article shall not apply to temporary loans made under article twenty-five, unless otherwise provided in said article.

Temporary loans excepted.

2937. *For what purposes bonds may be issued.* A municipality may issue its negotiable bonds for any one or more of the following purposes:

Purposes of bond issue.

1. For any purpose or purposes for which it may raise or appropriate money, except for current expenses.

Current expenses barred.

2. To fund or refund a debt of the municipality incurred before December fifth, nineteen hundred and twenty-one, if such debt be payable at the time of the passage of the ordinance authorizing bonds to fund or refund such debt or be payable within one year thereafter, or if such debt, although payable more than one year thereafter, is to be canceled prior to its maturity and simultaneously with the issuance of the bonds to fund or refund such debt: *Provided, however,* that bonds shall not be issued to refund serial bonds which mature in installments as provided in section two thousand nine hundred and fifty-two.

To fund or refund debts heretofore incurred.

Proviso: Serial bonds not refunded.

2938. Ordinance for bond issue:

1. *Ordinance required.* All bonds of a municipality shall be authorized by an ordinance passed by the governing body.

Bond issues to be ordered by ordinance.

2. *What ordinance must show.* The ordinance shall state:

Ordinance shall state:

a. In brief and general terms the purpose for which the bonds are to be issued;

Purpose of issue.

b. The maximum aggregate principal amount of the bonds;

Maximum amount.

c. That a tax sufficient to pay the principal and interest of the bonds shall be annually levied and collected;

Tax for principal and interest.

d. That a statement of the debt of the municipality has been filed with the clerk and is open to public inspection.

Statement of debt.

e. One of the following provisions:

(1) If the bonds are funding or refunding bonds or for local improvements of which at least one-fourth of the cost, exclusive of the cost of paving at street intersections, has been or is to be specially assessed, that the ordinance shall take effect upon its passage, and shall not be submitted to the voters; or

Ordinances taking effect on passage.

(2) If the bonds are for a purpose other than the payment of necessary expenses, or if the governing body, although not required to obtain the assent of the voters before issuing the bonds, deems it advisable to obtain such assent, that the ordinance shall take effect when approved by the voters of the municipality at an election as provided in this act; or

Ordinances taking effect on approval of voters.

(3) In any other case, that the ordinance shall take effect thirty days after its first publication (or posting) unless in the meantime a petition for its submission to the voters is filed under

Ordinances taking effect thirty days after publication.

this act, and that in such event it shall take effect when approved by the voters of the municipality at an election as provided in this act.

Where ordinances effective.

3. *When the ordinance takes effect.* A bond ordinance shall take effect at the time and upon the conditions indicated therein. If the ordinance provides that it shall take effect upon its passage no vote of the people shall be necessary for the issuance of the bonds.

Specifications of contemplated improvements.

4. *Need not specify location of improvement.* In stating the purpose of a bond issue, a bond ordinance need not specify the location of any improvement or property, or the kind of pavement or other material to be used in the construction or reconstruction of streets, highways, sidewalks, curbs, or gutters, or the kind of construction or reconstruction to be adopted for any building, for which the bonds are to be issued. A description in a bond ordinance of a property or improvement, substantially in the language employed in sections two thousand nine hundred and forty-two of this subchapter to describe such a property or improvement, shall be a sufficiently definite statement of the purpose for which the bonds authorized by the ordinance are to be issued.

Bonds for unrelated purposes.

2939. *Ordinance not to include unrelated purposes.* Bonds for two or more unrelated purposes, not of the same general class or character, shall not be authorized by the same ordinance: *Provided, however,* that bonds for two or more improvements or properties mentioned together in any one clause of subsection four of section two thousand nine hundred and forty-two of this subchapter may be treated as being but for one purpose, and may be authorized by the same bond ordinance. After two or more bond ordinances have been passed, the governing body may, in its discretion, direct all or any of the bonds authorized by the ordinances to be actually issued as one consolidated bond issue.

Proviso: Bonds for separate improvements of like character.

Consolidation of bond issues.

2940. (*Obsolete.*)

Bond ordinance before filing of petitions for improvements.

2941. *Ordinance and bond issue; when petition required.* In cases where a petition of property owners is required by law for the making of local improvements, a bond ordinance authorizing bonds for such local improvements may be passed before any such petition is made, but no bonds for the local improvements in respect of which such petitions are required shall be issued under the ordinance, nor shall any temporary loan be contracted in anticipation of the issuance of such bonds, unless and until such petitions are made, and then only up to the actual or estimated amount of the cost of the work petitioned for. The determination of the governing body as to the actual or estimated cost of work so petitioned for shall be conclusive in any action involving the validity of bonds or notes or other indebtedness. The bond ordinance may be made to take effect upon its passage, notwithstanding that the necessary petitions for the local improvements have not been filed: *Provided,* that it appears upon the face of the ordinance that one-fourth or some greater proportion of the cost, exclusive of the cost of work at street intersections, has been or is to be assessed.

Bonds not issued nor loans contracted until petitions filed.

Determination of cost of work.

Bond ordinance effective from passage.

Proviso: Special assessments.

2942. Determining periods for bonds to run:

Maturity of bonds.

1. *How periods estimated.* Either in the bond ordinance or in a resolution passed after the bond ordinance but before any bonds are issued thereunder, the governing body shall, within the limits prescribed by subsection four of this section, determine and declare:

Governing body to determine and declare.

a. The probable period of usefulness of the improvements or properties for which the bonds are to be issued; or

Probable life of improvements and properties.

b. If the bonds are to be funding or refunding bonds, either the shortest period in which the debt to be funded or refunded can be finally paid without making it unduly burdensome upon the taxpayers of the municipality, or, at the option of the governing body, the probable unexpired period of usefulness of the improvement or property for which the debt was incurred.

Term of funding or refunding bonds.

Unexpired life of improvements.

2. In the case of a consolidated bond issue comprising bonds authorized by different ordinances for different purposes, and in the case of a bond issue authorized by but one ordinance for several related purposes in respect of which several different periods are determined as aforesaid, the governing body shall also determine the average of the different periods so determined, taking into consideration the amount of bonds to be issued on account of each purpose or item in respect of which a period is determined.

Averages in consolidated issues.

The period required to be determined as aforesaid shall be computed from a date not more than one year after the time of passage of any bond ordinance authorizing the issuance of the bonds. The determination of any such period by the governing body shall be conclusive.

Computation of period.

Determinations conclusive.

3. *Maturity of bonds.* The bonds must mature within the period determined as aforesaid, or, if several different periods are so determined, then within said average period.

Maturity of bonds.

4. *Periods of usefulness.* In determining, for the purpose of this section, the probable period of the usefulness of an improvement or property, the governing body shall not deem said period to exceed the following periods for the following improvements and properties, respectively, viz.:

Periods of usefulness.

a. Sewer systems (either sanitary or surface drainage), forty years.

Sewer systems.

b. Water supply systems, or combined water and electric light systems, or combined water, electric light, and power systems, forty years.

Water, light, and power systems.

c. Gas systems, thirty years.

Gas systems.

d. Electric light and power systems, separate or combined, thirty years.

Electric light and power systems.

e. Plants for the incineration or disposal of ashes, or garbage, or refuse (other than sewage), twenty years.

Crematories.

f. Public parks (including or not including a playground, as a part thereof, and any buildings thereon at the time of acquisition thereof, or to be erected thereon, with the proceeds of the bonds issued for such public parks), fifty years.

Public parks.

g. Playgrounds, fifty years.

Playgrounds.

h. Buildings for purposes not stated in this section, if they are:

Buildings:

(1) Of fireproof construction, that is, a building the walls of which are constructed of brick, stone, iron, or other hard, incombustible materials, and in which there are no wood beams or lintels, and in which the floors, roofs, stair halls, and public halls are built entirely of brick, stone, iron, or other hard, incombustible materials, and in which no woodwork or other inflammable materials are used in any of the partitions, floorings, or ceiling (but the building shall be deemed to be of fireproof construction notwithstanding that elsewhere than in the stair halls and entrance halls there is wooden flooring on top of the fireproof floor, and that wooden sleepers are used, and that it contains wooden handrails

Of fireproof construction.

and treads, made of hardwood, not less than two inches thick), forty years.

Nonfireproof construction.

(2) Of nonfireproof construction, that is, a building the outer walls of which are constructed of brick, stone, iron, or other hard, incombustible materials, but which in any other respect differs from a fireproof building as defined in this section, thirty years.

Of other construction.

(3) Of other construction, twenty years.

Bridges and culverts.

i. Bridges and culverts (including retaining walls and approaches), forty years, unless constructed of wood, and in that case, ten years.

Lands.

j. Lands for purposes not stated in this section, fifty years.

Roads, streets or highways.

k. Constructing or reconstructing the surface of roads, streets, or highways, whether including or not including contemporaneous constructing or reconstructing of sidewalks, curbs, gutters, or drains, and whether including or not including grading, if such surface:

Sand and gravel.

(1) Is constructed of sand and gravel, five years;

Waterbound macadam.

(2) Is of waterbound macadam or penetration process, ten years;

Bricks, blocks, asphalt, or concrete.

(3) Is of bricks, blocks, sheet asphalt, bitulithic, or bituminous concrete, laid on a solid foundation, or is of concrete, twenty years.

Lands.

l. Land for roads, streets, highways, or sidewalks, or grading, or constructing or reconstructing culverts, or retaining walls, or surface, or subsurface drains, fifty years.

Sidewalks.

m. Constructing sidewalks, curbs, or gutters of brick, stone, concrete, or other material of similar lasting character, twenty years.

Systems of communication.

n. Installing fire or police alarms, telegraph or telephone service, or other system of communication for municipal use, thirty years.

Fire engines and other vehicles.

o. Fire engines, fire trucks, hose carts, ambulances, patrol wagons, or any vehicles for use in any department of the municipality, or for the use of municipal officials, ten years.

Land for cemeteries.

p. Land for cemeteries, or the improvement thereof, thirty years.

Service mains.

q. Constructing sewer, water, gas, or other service connections, from the service main in the street to the curb or property line, when the work is done by the municipality in connection with any permanent improvement of or in any street, ten years.

Elimination of grade crossings.

r. The elimination of any grade crossing or crossings and improvements incident thereto, thirty years.

Other equipment, apparatus, or furnishings.

s. Equipment, apparatus, or furnishings not included in the foregoing clauses of this subsection, ten years.

Other improvements or properties.

t. Any improvement or property not included in other clauses of this subsection, forty years.

Properties to which periods are applicable.

5. *Improvements and properties defined.* The maximum periods fixed herein for the improvements and properties mentioned in clauses numbered from *a* to *i*, both inclusive, of subsection 4 of this section shall be applied thereto whether such improvements or properties are to be acquired, constructed, reconstructed, enlarged, or extended, in whole or in part, and whether the same are to include or are not to include buildings, lands, rights in lands, furnishings, equipment, machinery, or apparatus constituting a part of said improvements or properties at the time of acquisition, construction, or reconstruction. If the improvements of properties are to be an enlargement or extension of existing properties or improvements, the probable period of usefulness to be determined

Enlargements and extensions.

as aforesaid may be either that of the existing properties or improvements; or that of the enlargement or extension. Bonds for any or all improvements or properties included in any one clause of subsection 4 above may for the purposes of this section be deemed by the governing body to be for but one improvement or property. Bonds for improvements of like classification.

6. *Kind of construction determined.* If the bonds are for a building referred to in clause *h* of subsection 4 above, and the bond ordinance does not state the kind of construction of the building, or if the bonds are for street improvements mentioned in clause *k* of subsection 4 above, and the bond ordinance does not state the kind or kinds of pavement or other material to be used, then the kind of construction, or the kind or kinds of pavement or other material, as the case may be, shall be determined by resolution before any of the bonds are issued. Determination of classification.

7. *Shortest period of payment.* In determining, for the purpose of this section, the shortest period in which a debt to be funded or refunded hereunder can be finally paid without making it unduly burdensome upon the taxpayers of the municipality, the governing body shall not deem said period to be greater than the following periods in the following cases, respectively: Determination of shortest period of payment.

a. Thirty years, if funding bonds are to be issued. Thirty years.

b. Thirty years, if refunding bonds are to be issued, and the net debt of the municipality, as stated in the debt statement filed pursuant to section two thousand nine hundred and forty-three, is not more than four per centum of the assessed valuation set forth in said statement. Thirty years.

c. Forty years, if refunding bonds are to be issued, and said net debt is more than four but not more than five per centum of said assessed valuation. Forty years.

d. Fifty years, if refunding bonds are to be issued, and said net debt is more than five per centum of said assessed valuation. Fifty years.

2943. Sworn statement of indebtedness:

1. *What shall be shown.* After the introduction and before the final passage of a bond ordinance an officer designated by the governing body for that purpose shall file with the clerk a statement showing the following: Statements to be filed before passage of ordinance.

(*a*) The gross debt (which shall not include debt incurred or to be incurred in anticipation of the collection of taxes or in anticipation of the sale of bonds other than funding and refunding bonds), which gross debt shall be as follows: Gross debt.

(1) Outstanding debt incurred before December sixth, one thousand nine hundred and twenty-one, not evidenced by bonds. Outstanding floating debt.

(2) Outstanding bonded debts. Outstanding bond debt.

(3) Bonded debt to be incurred under ordinances passed or introduced. Bonded debt to be incurred.

(*b*) The deductions to be made from gross debt in computing net debt, which deductions shall be as follows: Deductions.

(1) Amount of unissued funding or refunding bonds included in gross debt. Unissued funding bonds.

(2) Amount of sinking funds or other funds held for the payment of any part of the gross debt other than debt incurred for water, gas, electric light, or power purposes or two or more of said purposes. Amount of sinking fund or other funds.

(3) The amount of uncollected special assessments theretofore levied on account of local improvements for which any part of the Uncollected special assessments.

gross debt was or is to be incurred which will be applied when collected to the payment of any part of the gross debt.

Amount of special assessments to be levied.

(4) The amount, as estimated by the engineer of the municipality or officer designated for that purpose by the governing body or by the governing body itself, of special assessments to be levied on account of local improvements for which any part of the gross debt was or is to be incurred, and which, when collected, will be applied to the payment of any part of the gross debt.

Bonded debt for water, gas, light, and power systems.

(5) The amount of bonded debt included in the gross debt and incurred, or to be incurred, for water, gas, electric light or power purposes, or two or more of said purposes.

Net debt.

(*c*) The net debt, being the difference between the gross debt and the deductions.

Assessed valuation of property.

(*d*) The assessed valuation of property as last fixed for municipal taxation.

Percentage.

(*e*) The percentage that the net debt bears to said assessed valuation.

Limitation.

2. *Limitations upon passage of ordinance.* The ordinance shall not be passed unless it appears from said statement that the said net debt does not exceed eight (8) per cent of said assessed valuation, unless the bonds to be issued under the ordinance are to be funding or refunding bonds, or are bonds for water, gas, electric light or power purposes, or two or more of said purposes.

Statements filed for inspection. Statements deemed true.

3. *Statement filed for inspection.* Such statements shall remain on file with the clerk and be open to public inspection. In any action or proceeding in any court involving the validity of bonds, said statement shall be deemed to be true and to comply with the provisions of this act, unless it appears (in an action or proceeding commenced within the time limited by section 2945 for the

Impeachment of statements.

commencement thereof), first, that the representations contained therein could not by any reasonable method of computation be true; and second, that a true statement would show that the ordinance authorizing the bonds could not be passed.

Publication of bond ordinance.

2944. *Publication of bond ordinance.* A bond ordinance shall be published once in each of two successive weeks after its final passage. A notice substantially in the following form (the blanks being first properly filled in), with the printed or written signature of the clerk appended thereto, shall be published with the ordinance:

Form of notice.

The foregoing ordinance was passed on the....day of....., 19...., and was first published (or posted), on the.....day of ....., 19....

Any action or proceeding questioning the validity of said ordinance must be commenced within thirty days after its first publication (or posting).

....,
Clerk (or Secretary).

Limitation of action.

2945. *Limitation of action to set aside ordinance.* Any action or proceeding in any court to set aside a bond ordinance, or to obtain any other relief upon the ground that the ordinance is invalid, must be commenced within thirty days after the first publication of the notice aforesaid and the ordinance or supposed ordinance

Actions barred.

referred to in the notice. After the expiration of such period of limitation, no right of action or defense founded upon the in-

validity of the ordinance shall be asserted, nor shall the validity of the ordinance be open to question in any court upon any ground whatever, except in an action or proceeding commenced within such period.

2946. (*Obsolete.*)

2947. Ordinance requiring popular vote:

1. *Petition filed.* A petition demanding that a bond ordinance be submitted to the voters may be filed with the clerk within thirty days after the first publication of the ordinance. The petition shall be in writing and signed by voters of the municipality equal in number to at least twenty-five per centum of the total number of registered voters in the municipality as shown by the registration books for the last preceding election for municipal officers therein. The residence address of each signer shall be written after his signature. Each signature to the petition shall be verified by a statement (which may relate to a specified number of signatures), made by some adult resident freeholder of the municipality, under oath before an officer competent to administer oaths, to the effect that the signature was made in his presence and is the genuine signature of the person whose name it purports to be. The petition need not contain the text of the ordinance to which it refers. The petition need not be all on one sheet, and if on more than one sheet, it shall be verified as to each sheet.

Petition for election.

Specification of requirements.

Verification of signatures.

Need not contain text.

Separate sheets.

3. *Sufficiency of petitions.* The clerk shall investigate the sufficiency of the petition and present it to the governing body with a certificate stating the result of his investigation. The governing body shall thereupon determine the sufficiency of the petition and the determination of the governing body shall be conclusive.

Clerk to investigate sufficiency of petition.

Determination of sufficiency.

2948. Elections on bond issue:

1. *What majority required.* If a bond ordinance provides for the issuance of bonds for a purpose other than the payment of necessary expenses of the municipality, the approval of a majority of the qualified voters of the municipality, as required by the Constitution of North Carolina, shall be necessary in order to make the ordinance operative. If, however, the bonds are to be issued for necessary expenses, the affirmative vote of the majority of the voters voting on the bond ordinance shall be sufficient to make it operative, in all cases where the ordinance is required by this act to be submitted to the voters.

Majority of registered voters.

Majority of votes cast.

2. *When election held.* Whenever the taking effect of an ordinance authorizing the issuance of bonds is dependent upon the approval of the ordinance by the voters of a municipality, the governing body may submit the ordinance to the voters at an election to be held not more than six months after the passage of the ordinance. The governing body may call a special election for that purpose or may submit the ordinance to the voters at the regular municipal election next succeeding the passage of the ordinance, but no such special election shall be held within one month before or after a regular election. Several ordinances or other matters may be voted upon at the same election.

Time for election.

Special elections.

Limitations.

Separate matters voted on.

3. *New registration.* The governing body of the city or town in which such election is held may, in their discretion, order a new registration of the voters for such election. The books for such new registration shall remain open in each precinct from nine a. m. to six p. m. on each day, except Sundays and holidays, for three weeks, beginning on a Monday morning and ending on the second

New registration.

Time of registration.

Election officers.

Saturday evening before the election. A registrar and two judges of election shall be appointed by the governing body for each precinct: *Provided,* that the books shall be open at the polling places on each Saturday during the registration period. Sufficient notice shall be deemed to have been given of such new registration and of the appointment of the election officers if a notice thereof be published at least thirty (30) days before the closing of the registration books, stating the hours and days for registration. It shall not be necessary to specify in said notice the places for registration. In case the registrar shall fail or refuse for any cause to perform his duties, it shall be lawful for the clerk to appoint another person to perform such duties, and no notice of such appointment shall be necessary.

Proviso: Registration on Saturdays.

Sufficiency of notice.

Change of register.

Notice of election.

4. *Notice of election.* A notice of the election shall be deemed sufficiently published if published once not later than twenty days before the election. Such notice shall state the maximum amount of the proposed bonds and the purpose thereof, and the fact that a tax will be levied for the payment thereof. The date of the election shall be stated therein.

Statements to be made.

Ballots.

5. *Ballots.* A ballot or ballots shall be furnished to each qualified voter at said election, which ballots may contain the words "for the ordinance authorizing $..... bonds (briefly stating the purpose), and a tax therefor," and "against the ordinance authorizing $..... bonds (briefly stating the purpose), and a tax therefor," and if one ballot contains the two alternatives it may contain squares in one of which the voter may make a (X) mark, but this form of ballot is not prescribed.

Return of votes.

6. *Returns canvassed.* The officers appointed to hold the election in making return of the result thereof, shall incorporate therein not only the number of votes cast for and against each ordinance submitted, but also the number of voters registered and qualified to vote in the election. The governing body shall canvass the returns, and shall include in their canvass the votes cast and the number of voters registered and qualified to vote in the election, and shall judicially determine and declare the result of the election.

Canvass of returns.

Application of general law.

7. *Application of other laws.* Except as herein otherwise provided, the registration and election shall be conducted in accordance with the laws then governing elections for municipal officers in such municipality, and governing the registration of the electors for such election of officers.

Certificate of result.

8. *Statement of result.* The board shall prepare a statement showing the number of votes cast for and against each ordinance submitted, and the number of voters qualified to vote in the election, and declaring the result of the election, which statement shall be signed by a majority of the members of the board and delivered to the clerk of the municipality, who shall record it in the book of ordinances of the municipality and file the original in his office and publish it once.

Record of certificate. Original filed.

Limitation of actions as to election.

9. *Limitation as to actions.* No right of action or defense founded upon the invalidity of the election shall be asserted, nor shall the validity of the election be open to question in any court upon any ground whatever, except in an action or proceeding commenced within thirty days after the publication of such statement: *Provided,* that sections 2947 and 2948 shall not apply to the incorporated towns of Madison County.

Proviso: towns excepted.

2949. *Preparation for issuing bonds.* At any time after the passage of a bond ordinance, all steps preliminary to the actual issuance of bonds under the ordinance may be taken, but the bonds shall not be actually issued unless and until the ordinance takes effect. Preparation for bond issue.

2950. *Within what time bonds issued.* After a bond ordinance takes effect, bonds may be issued in conformity with its provisions at any time within three years after the ordinance takes effect, unless the ordinance shall have been repealed, which repeal is permitted (without the privilege of referendum upon the question of appeal), unless notes shall have been issued on anticipation of the receipts of the proceeds of the bonds and shall be outstanding. Time for issuance of bonds. Repeal of ordinance. Notes barring repeal.

2951. *Amount and nature of bonds determined.* The aggregate amount of bonds to be issued under a bond ordinance, the rate or rates of interest they shall bear, not exceeding six per centum per annum, payable semi-annually, and the times and place or places of payment of the principal and interest of the bonds, shall be fixed by resolution or resolutions of the governing body. The bonds may be issued either all at one time or from time to time in blocks, and different provisions may be made for different blocks. Determination of terms of bonds.

2952. *Bonded debt payable in installments.* Each bond issue made under this act shall mature in annual installments or series, the first of which shall be made payable not more than three years after the date of the first issued bonds of such issue, and the last within the period determined and declared pursuant to section two thousand nine hundred and forty-two of this subchapter. No such installment or series shall be more than two and one-half times as great in amount as the smallest prior installment or series of the same bond issue. If all of the bonds of an issue are not issued at the same time, the bonds at any one time outstanding shall mature as aforesaid. Bonds payable in installments. Times of maturity. Proportion of installments. Bonds issued at intervals.

2953. *Medium and place of payment.* The bonds may be made payable in such kinds of money and at such place or places within or without the State of North Carolina as the governing body may by resolution provide. Medium and place of payment.

2954. *Formal execution of bonds.* The bonds shall be issued in such form as the officers who execute them shall adopt, except as otherwise provided by the governing body. They shall be signed by two or more officers designated by the governing body, or, if the governing body makes no such designation, then by the mayor or other chief executive officer and by the clerk, and the corporate seal of the municipality shall be affixed to the bonds. The bonds may have coupons attached for the interest to be paid thereon, which coupons shall bear a facsimile signature of the clerk in office, at the date of the bonds or at the date of delivery thereof. The delivery of bonds so executed shall be valid notwithstanding any change in the officers or in the seal of the municipality occurring after the signing and sealing of the bonds. Form of bonds. Execution. Coupons. Delivery.

2955. Registration and transfer of bonds:

1. *Bonds payable to bearer.* Bonds issued under this act shall be payable to the bearer unless they are registered as provided in this section; and each coupon appertaining to a bond shall be payable to the bearer of the coupon. Bonds and coupons payable to bearer.

Registration or transfer agent.

Bonds registered at request of owner.

Payable to registered owner.

2. *Registration and effect.* A municipality may keep in the office of its financial officer or in the office of a bank or trust company appointed by the governing body as bond registrar or transfer agent, a register or registers for the registration and transfer of its bonds, in which it may register any bond at the time of its issue, or, at the request of the holder, thereafter. After such registration the principal and interest of the bond shall be payable to the person in whose name it is registered except in the case of a coupon bond registered as to principal only, in which case the principal shall be payable to such person, unless the bond shall be discharged from registry by being registered as payable to bearer. After registration a bond may be transferred on such register by the registered owner in person or by attorney, upon presentation to the bond registrar, accompanied by delivery of a written instrument of transfer in a form approved by the bond registrar, executed by the registered owner.

Transfer of registered bonds.

Registration and transfer noted on bonds.

Coupons canceled on registration of bonds.

3. *Registration and transfer noted on bond.* Upon the registration or transfer of a bond as aforesaid, the bond registrar shall note such registration or transfer on the back of the bond. Upon the registration of a coupon bond as to both principal and interest he shall also cut off and cancel the coupons.

Recital of agreement in bonds.

4. *Agreement for registration.* A municipality may, by recital in its bonds, agree to register the bonds as to principal only, or agree to register them either as to principal only or as to both principal and interest at the option of the bondholder.

Sale below par forbidden.

2956. *Sale of bonds.* All bonds of a municipality shall be sold at not less than par. They shall be advertised and sold upon sealed proposals, or at public auction, unless the sale is made within thirty days after failure to receive any legally acceptable bid in response to a public offering made as provided in this section.

Advertisement of sale.

Whenever bonds are to be sold pursuant to advertisement, there shall be published, at least once, a notice containing a description of the bonds to be sold, the place of sale, and the time of sale, or time limited for the receipt of proposals, which shall be not less than ten days after the first publication of the notice. The notice shall state that bidders must present with their bids a certified check upon an incorporated bank or trust company, payable to the order of the municipality or of an executive, financial or clerical officer thereof, or a sum of money for or in an amount equal to two (2) per centum of the face amount of bonds bid for, to secure the municipality against any loss resulting from a failure of the bidder to comply with the terms of his bid. The said notice shall be published not only in the manner prescribed by section two thousand nine hundred and twenty, but also at least ten days before the expiration of the time limited for the receipt of bids, in a financial paper or trade journal published within the State of North Carolina, which publishes from time to time notices of the sale of municipal bonds; and the determination of the governing body that the paper or journal named for said publication is such financial paper or trade journal, and that it publishes from time to time notices of the sale of municipal bonds shall be conclusive.

Guaranty of bids.

Publication of notice.

Determination as to financial or trade journal.

Bids opened.

Awarded.

Delegation of powers.

Proposals submitted pursuant to such notices shall be opened in public and the bonds shall be awarded to the highest bidder, unless all bids are rejected. The governing body may delegate the power to sell bonds to a committee thereof, or any two offi-

cers, but every private sale of bonds shall be made or confirmed by the governing body. Bonds of the municipality sold out of a sinking fund of a municipality shall be sold as provided in this section, except that such bonds may be sold for less than par.

Confirmation of sales.

Sales out of sinking fund.

Nothing herein shall prevent a municipality from awarding its bonds to the bidder offering to take them at the lowest rate of interest, provided the notice of sale invites bidders to name rate of interest which the bonds are to bear.

Sales at lowest interest.

2957. *Application of funds.* The proceeds of the sale of bonds under this act shall be used only for the purposes specified in the ordinance authorizing said bonds, and for the payment of the principal and interest of temporary loans made in anticipation of the sale of bonds: *Provided, however,* that if for any reason any part of such proceeds are not applied to or are not necessary for such purposes, such unexpended part of the proceeds shall be applied to the payment of the principal or interest of said bonds. The cost of preparing, issuing, and marketing bonds shall be deemed to be one of the purposes for which the bonds are issued.

Application of proceeds.

Proviso: Balance to purchase of bonds.

Cost of preparation issue, and marketing.

2958. *Bonds incontestable after delivery.* Any bonds reciting that they are issued pursuant to this act shall in any action or proceeding involving their validity be conclusively deemed to be fully authorized by this act, and to have been issued, sold, executed, and delivered in conformity herewith, and with all other provisions of statutes applicable thereto, and shall be incontestable, anything herein or in other statutes to the contrary notwithstanding, unless such action or proceeding is begun prior to the delivery of such bonds.

Bonds incontestable after delivery.

2959. *Taxes levied for payment of bonds.* The full faith and credit of the municipality shall be deemed to be pledged for the punctual payment of the principal of and interest on every bond and note issued under this act, including assessment bonds or other bonds for which special funds are provided. The governing body shall annually levy and collect a tax ad valorem upon all the taxable property in the municipality sufficient to pay the principal and interest of all bonds issued under this act as such principal and interest become due: *Provided, however,* that such tax may be reduced by the amount of other moneys appropriated and actually available for such purpose.

Faith and credit pledged for payment.

Taxes.

Proviso: Reduction of tax.

So much of the net revenue derived by the municipality in any fiscal year from the operation of any revenue producing enterprise owned by the municipality after paying all expenses of operating, managing, maintaining, repairing, enlarging, and extending such enterprise, shall be applied, first to the payment of the interest, payable in the next succeeding year on bonds issued for such enterprise, and next, to the payment of the amount necessary to be raised by tax in such succeeding year for the payment of the principal of said bonds. All money derived from the collection of special assessments for local improvements for which bonds or notes were issued shall be placed in a special fund and used only for the payment of bonds or notes issued for the same or other local improvements.

Application of revenue from bonded enterprises.

Application of special assessments.

Every municipality shall have the power to levy taxes ad valorem upon all taxable property therein for the purpose of paying the principal of or the interest on any bonds or notes for the payment of which the municipality is liable, issued under any act other than this act, or for the purpose of providing a

Power to levy taxes.

sinking fund for the payment of said principal, or for the purpose of paying the principal of or interest on any notes issued under this act.

Taxes for payment of bonds not subject to limitations.

The powers stated in this section in respect of the levy of taxes for the payment of the principal and interest of bonds and notes shall not be subject to any limitation prescribed by law upon the amount or rate of taxes which a municipality may levy.

Levy and collection of taxes.

Taxes levied under this section shall be levied and collected in the same manner as other taxes are levied and collected upon property in the municipality.

Restrictions on powers as to:

Article 27. Restrictions Upon the Exercise of Municipal Powers.

2960. In borrowing or expending money:

1. No municipality shall:

Appropriations.

a. Make an appropriation of money except as provided in this act;

Incurring debt.

b. Borrow money or issue bonds or notes except as provided in this act;

Expenditures.

c. Make an expenditure of money unless the money shall have been appropriated as provided in this act, or unless the expenditure is a payment of a judgment against the municipality or is a payment of the principal or interest of a bond or note of the municipality; or,

Entrance into contracts.

d. Enter into any contract involving the expenditure of money unless a sufficient appropriation shall have been made therefor, except a continuing contract to be performed in whole or in part in an ensuing fiscal year, in which case an appropriation shall be made sufficient to meet the amount to be paid in the fiscal year in which the contract is made.

Authorization of bond issue and appropriation.

2. The authorization of bonds by a municipality shall be deemed to be an appropriation of the maximum authorized amount of the bonds for the purposes for which they are to be issued.

Passage of ordinances and resolutions.

2961. *Manner of passing ordinances and resolutions.* Ordinances and resolutions passed pursuant to this act shall be passed in the manner provided by other laws for the passage of ordinances and resolutions, but shall not be subject to the provisions of other laws prescribing conditions, acts, or things necessary to exist, happen, or be performed precedent to or after the passage of ordinances or resolutions in order to give them full force and effect: *Provided, however,* that in any municipality in which the acts of the governing body thereof involving the raising or expenditure of money are required by law to be approved by some other official board or officer of the municipality in order to make them effective, all ordinances and resolutions passed by the governing body under this act shall, unless they relate solely to elections held under this act, be so approved before they take effect.

Proviso: Approval of acts and ordinances.

Enforcement of orders of court.

2962. *Enforcement of act.* If any board or officer of a municipality shall be ordered by a court of competent jurisdiction to levy or collect a tax to pay a judgment or other debt, or to perform any duty required by this act to be performed by such board or officer, and shall fail to carry out such order, the court, in addition to all other remedies, may appoint its own officers or other persons to carry out such order.

2963. *Limitation of tax for general purposes.* For the purpose of raising revenue for defraying the expenses incident to the proper government of the municipality, the governing body shall have the power and it is hereby authorized to levy and collect an annual ad valorem tax on all taxable property in the municipality at a rate not exceeding one dollar on the one hundred dollars valuation of said property, notwithstanding any other law, general or special, heretofore or hereafter enacted, except a law hereafter enacted expressly repealing or amending this section: *Provided,* that in cities where the taxable values for the year 1920 amounted to one hundred million dollars or more, the rate of taxation for general purposes shall not exceed sixty-five (65) cents on the one hundred dollars valuation.

Tax for general purposes.

Limit of rate.

Proviso: Rate in larger cities.

2964. *Certain taxes validated.* All taxes levied by any municipality after the enactment of chapter one hundred and thirty-eight of public laws of one thousand nine hundred and seventeen, and prior to December sixth, one thousand nine hundred and twenty-one, are hereby ratified and validated, notwithstanding the rate of said taxes exceeded the maximum rate prescribed by law, or any other defect or irregularity in the levy thereof.

Certain taxes validated.

2965. *Outstanding floating debt validated, and may be funded.* All floating or other indebtedness, not evidenced by bonds, which was outstanding on December sixth, one thousand nine hundred and twenty-one, and was incurred by a municipality in good faith for necessary expenses thereof (including floating or other indebtedness incurred in anticipation of the collection of taxes or for current expenses) is hereby validated, notwithstanding any want of power or authority to incur indebtedness for the purpose for which such indebtedness was incurred, and notwithstanding any defect in the procedure for incurring indebtedness, or any other defect or illegality, including the failure to observe any debt limit prescribed by law. The municipality may fund such outstanding indebtedness by issuing bonds as herein provided.

Outstanding debts validated.

Power to fund debt.

2966-2969, inclusive (obsolete).

SEC. 2. All acts and parts of acts, whether general, special, private or local, regulating or relating in any way to the issuance of bonds or other obligations of a municipality, or relating to the subject-matter of this act, are hereby repealed: *Provided, however,* that this act shall not affect any local or private act enacted at the present session of the General Assembly, or regular session of one thousand nine hundred and twenty-one, but the powers hereby conferred and the methods of procedure hereby provided shall be deemed to be conferred and provided in addition to and not in substitution for those conferred or provided by any such local or private act enacted at the present session of the General Assembly, or regular session of one thousand nine hundred and twenty-one, so that any municipality may, at its option, proceed under any such local or private act applicable to it enacted at the present session of the General Assembly or regular session of one thousand nine hundred and twenty-one without regard to the restrictions imposed by this act, or may proceed under this act without regard to the restrictions imposed by any other act: *Provided further,* that this act shall not affect any of the provisions of article nine of subchapter one of chapter fifty-six of the Consolidated Statutes (originally chapter fifty-six of the

Repealing clause.

Proviso: Local and private acts.

Powers additional.

Proviso: Acts not affected.

Public Laws of one thousand nine hundred and fifteen), except those provisions which prescribe methods of procedure for borrowing money or issuing bonds or other obligations, and said article shall apply to all municipalities in this State, notwithstanding any inconsistent, general, special, local or private laws:

Proviso: Action heretofore had.

Provided further, that this act shall not affect any acts or proceedings heretofore done or taken for the issuance of bonds or other obligations under the Municipal Finance Act, as it stood prior to the ratification of this act or under any other act, and every municipality is hereby authorized to complete said acts and proceedings pursuant to the acts under which they were done or taken, and to issue said bonds or other obligations under such acts in the same manner as if this act had not been passed:

Proviso: Bonds and notes not invalidated.

Provided further, that this act shall not render invalid any bonds or notes or proceedings for the issuance of bonds or notes in cases where such bonds, notes or proceedings have been validated by any other act.

Specific repeal.

SEC. 3. The whole of chapter three of the Public Laws of one thousand nine hundred and twenty, extra session, except section six thereof, is hereby repealed.

Printing and distribution of act.

SEC. 4. Immediately upon the ratification of this act, the Secretary of State shall cause to be printed in pamphlet form at least one thousand five hundred copies hereof, and to cause a copy of such pamphlet to be mailed to every city and town in this State.

SEC. 5. That this act shall be in full force from and after its ratification.

Ratified this the 20th day of December, A.D. 1921.

Appendix C

DEFINITIONS OF TERMS USED IN INVESTMENT BANKING

Accrued interest.

The interest at the rate borne by the bond from the date of sale to the next coupon or interest payment date, or from the last interest or coupon date to date of settlement. In making computations the day of settlement is excluded.

All or none.

A condition imposed by the bidder for an issue or issues of securities by which all the bonds he bids for must be awarded to him, or none at all.

Amortization.

The payment of a debt by means of annual or periodic contributions to a sinking fund. In the case of bonds purchased at a premium, it is the setting aside from annual interest such an amount as is sufficient to make good the premium at the maturity of the bond.

Annual interest.

Interest payable once a year, which is not considered desirable.

Assessed valuation.

The valuation placed upon property for the purpose of determining the amount of the tax paid by the owner. While most statutes require that property shall be assessed at its full or true value, the assessed valuation is rarely the actual cash value. The term is used principally in connection with the assessed valuation of real estate.

Authorized issue.

The total amount of bonds which may be sold pursuant to the statute or ordinance authorizing them.

Average maturity.

Example: the average maturity of $20,000 bonds maturing $1,000 each year for twenty years, is ten years.

Basis.

The average annual percentage return upon the money invested.

Below par.

A price less than face value.

Bonded debt.

The gross bonded debt is the total of all outstanding bonds of the municipality. The net bonded debt is such total less sinking funds and funds on hand to pay maturing bonds. In computing net debt, particular attention must be given to the purpose for which such computation is made and statutory provisions strictly construed.

Callable.

Subject to call or redemption previous to the date of maturity. If a bond is callable, its price is based upon the term to the date when it may be called and not upon the term to maturity. Called bonds are those which have been called for redemption.

Carry.

A bank carries a broker's bonds when it makes a loan upon the bonds.

Certified.

Any fact which has been vouched for in writing. Thus the signatures and seal appearing upon a bond may be certified to be genuine by some bank or trust company. A legal paper is certified by the municipal clerk to be a true and correct copy of the original.

Charter.

The municipal charter is the grant of power to the municipality contained in the statutes enacted by the State legislature.

Coupons.

Promissory notes attached to a bond and forming a part of the instrument until detached, promising to pay a definite

amount of money on definite dates. The amount of money promised is the semi-annual or annual interest at the rate borne by the bond. A detached coupon is a separate and distinct promise to pay.

Coupon bonds.

Those having coupons attached.

Cremation certificate.

It sometimes happens that too many bonds of an issue are printed, and they may or may not be executed. In any event the surplus should be destroyed and this is ordinarily accomplished by burning them. A statement signed by the persons witnessing the destruction of them is made and filed with a designated depository. This frequently happens in connection with New Jersey serial bonds.

Currency bond.

One not payable in gold coin, but in lawful money.

Date of bond.

It is ordinarily immaterial whether or not bonds be dated on Sundays or holidays, the usual opinion to the contrary notwithstanding.

Debenture.

A bond which is not secured by a mortgage.

Definitive bonds.

The preparation of bonds is sometimes delayed, and in anticipation of their issue, temporary receipts are given to the purchaser. These are exchanged for the definitive bonds when the latter are ready for delivery.

Denomination.

The face value of a bond, ordinarily $1,000. Bonds of $500 and $100 denominations are sometimes issued, but this practice should be avoided.

Depreciation.

The amount charged off for wear and tear, obsolescence, and reduction in value of property.

Direct obligation.

The full unlimited and unqualified promise of the obligator in a bond or note, as used in connection with municipal securities, means that the bond is supported by the full taxing power of the municipality, operating upon all its taxable property. Distinguished from special assessment bonds and those issued by a municipal corporation for and on account of a tax district.

Discount.

The percentage or price of a security below the par or face value. If par is $100 and the bond sells at $95, the discount is 5 per cent, or $5.

Drawn bond.

One drawn by lot for payment before maturity.

Escrow.

Escrow is the practice of depositing papers or securities with a third party to be held until a designated event takes place. For example, a municipality may deposit its bonds with a bank, and the purchaser may pay the purchase price to the same bank, the transaction to be consummated when proof in stipulated form is deposited with the bank that no litigation exists with regard to the issuance of the securities or the purchase of property for which the bonds are issued.

Ex-coupon.

Without interest. Coupons already due or about to become due, detached.

Face value.

The equivalent of par because par does not always include accrued interest. If the bond is for $1000, its face value is the same.

Fiscal agent.

Banks in large cities or par points are sometimes designated by municipal corporations as fiscal agents. Such designations ordinarily mean only that the interest or principal of bonds will be paid at such bank. The term is larger than its application.

Fiscal year.

A yearly period, regardless of the calendar year, for which books are kept, or in the case of municipalities, for which provision for expenses is made.

Five-twenties.

Bonds due in twenty years, but callable after five years. (See *Callable.*)

Flat.

Without accrued interest.

Floating debt.

Notes, certificates, or short-term bonds, ordinarily issued to provide funds for running expenses, or in anticipation of the issue of permanent bonds. Distinguished from bonded debt.

Franchise.

A privilege granted by governmental authority, such as the right to form a corporation, or to place tracks in a street.

Funded debt.

Bonded debt permanent in its nature as distinguished from a temporary floating debt.

Funding.

The operation of converting floating indebtedness into funded debt.

Gold bonds.

Those payable in United States gold coin of the present standard of weight and fineness. If a bond is payable in gold, the salesman has an additional talking point, but a promise to pay in gold has no other value. The practice of making bonds payable in gold is largely abandoned.

Income basis or return.

See *Net return.*

Indorsed bond.

One upon which something has been written, such as the owner's name. Such a bond may not be a good delivery, that is, the intending purchaser is not obliged to accept it. Noth-

ing should be written upon a bond. If an assignment is necessary and no provision is made for it on the back of the bond, write the assignment on a separate paper and attach it to the bond.

Installment bonds.

See *Serial bonds.*

Interchangeable bonds.

A coupon bond may sometimes be surrendered and a new bond issued in registered form, and a registered bond surrendered and a new coupon bond issued in place of it. This is rare in the case of municipals.

Interest.

The price of money. The interest on a $1,000 bond at 5 per cent is $50 a year, which is the price the borrower pays for the use of the money for one year.

Issue price.

The price at which an issue of bonds is offered to the public.

Joint account.

Two or more persons, investment bankers or banks, may buy an issue of securities. This is sometimes called a syndicate. The partner having charge of the transaction is called the syndicate manager.

Judgment bonds.

Bonds issued to fund a judgment.

Lawful money.

This is money which the government declares to be legal tender in payment of obligations. Distinguished from gold coin.

Legal investments.

Those which the statutes and regulations of various States prescribe as being proper investments for savings banks and trustees. They sell at a better price than bonds not "legal."

Legal Rate of Interest.

A fixed maximum interest rate established by statute.

Lien.

A claim against property which the creditor may have applied to the satisfaction of a debt. A mortgage is a lien. A municipal bond is almost never a lien and the term should not be used in describing municipal bonds.

Market value.

The price which a security will probably bring if sold. The market value of a security listed on the New York Stock Exchange is easily determinable. The market value of municipal bonds depends upon the concensus of dealers' opinions.

Maturity.

The date when bonds are payable.

Negotiable instrument.

An obligation which may be transferred free from equitable defenses which the maker may have against the original holder.

Net debt.

See bonded debt.

Net price.

The lowest price, less discounts or other allowances.

Net return on investments.

The amount of return to the investor, taking into consideration interest rate, the price of the security, whether above or below par, and the term of the bond.

Premium.

The price of a security in excess of its par or face value. If a $1,000 bond sells for $1,090, the premium is $90.

Principal

The amount promised to be paid; the face value of a bond.

Quasi-municipal.

A term applied to water districts, irrigation districts and road districts.

Railroad-aid bonds.

Those issued by municipalities to raise funds to give financial assistance to a railroad. Fortunately now forbidden to be issued in most States.

Redeemable.

See *Callable.*

Refunding.

The issuing of new bonds to take the place of old ones.

Registered bond.

A bond payable to a designated payee. Such bonds may be registered both as to principal and interest, or registered as to principal only. Most municipal bonds are in the first instance issued as coupon bonds with the privilege of registration as to principal only, or as to both principal and interest. A registered bond can be transferred only by assignment and does not pass by delivery or endorsement.

Revenue bond.

One issued in anticipation of current taxes, or revenues.

Sealed bid.

A proposition to purchase bonds in response to an advertisement calling for such tender, is usually submitted in a sealed envelope, in order that bidders may not know the prices their competitors are willing to offer. Sealed bids are opened at one time, and no modification of such a bid can be made, after bids are opened.

Semi-annual interest.

Interest payable twice a year—as on January first and July first.

Serial bonds.

An issue of which the bonds are payable in installments. Thus an issue of $100,000 bonds payable $10,000 a year for ten years, is an issue of serial bonds.

Sinking fund.

This is a fund provided by contributions made at stated intervals to provide for the payment of the principal of the debt.

Special assessment bonds.

A bond payable from assessments and for which the credit of the issuing municipality may not be pledged. As it is a bond payable from a special fund, it may not be a negotiable instrument.

State bonds.

Those issued by one of the States of the Union.

Syndicate.

See *Joint account.*

Temporary certificates.

See *Definitive bonds.*

Ten-twenties.

Bonds due in twenty years but subject to redemption at or after ten years.

Warrant.

Municipal paper which is usually an order upon the treasurer for the payment of money.

When and as issued.

Sales of securities are sometimes made prior to the actual issue "when, as and if issued," to protect the seller from liability in case the securities are never issued.

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